S. Hrg. 104–840

PROPOSED CONSTITUTIONAL AMENDMENTS TO REQUIRE A TWO-THIRDS VOTE TO INCREASE TAXES AND TO PROHIBIT RETROACTIVE TAXATION

HEARING

BEFORE THE

SUBCOMMITTEE ON THE CONSTITUTION, FEDERALISM, AND PROPERTY RIGHTS

OF THE

COMMITTEE ON THE JUDICIARY UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

SECOND SESSION

ON

S.J. Res. 8

A RESOLUTION PROPOSING AN AMENDMENT TO THE CONSTITUTION OF THE UNITED STATES TO PROHIBIT RETROACTIVE INCREASES IN TAXES

S.J. Res. 49

A RESOLUTION PROPOSING AN AMENDMENT TO THE CONSTITUTION OF THE UNITED STATES TO REQUIRE TWO-THIRDS MAJORITIES FOR BILLS INCREASING TAXES

APRIL 15, 1996

Serial No. J–104–72

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PROPOSED CONSTITUTIONAL AMENDMENTS TO REQUIRE A TWO-THIRDS VOTE TO INCREASE TAXES AND TO PROHIBIT RETROACTIVE TAXATION

MONDAY, APRIL 15, 1996

U.S. SENATE,
SUBCOMMITTEE ON THE CONSTITUTION, FEDERALISM,
AND PROPERTY RIGHTS,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room SD–226, Dirksen Senate Office Building, Hon. Hank Brown (chairman of the subcommittee) presiding.

Also present: Senator Kyl.

OPENING STATEMENT OF HON. HANK BROWN, A U.S. SENATOR FROM THE STATE OF COLORADO

Senator BROWN. The subcommittee will come to order. The subject of the hearing is a constitutional amendment proposed by Senator Kyl that would change the way we have done business in this country for most of our history by imposing a super-majority standard of a two-thirds vote to effect tax increases.

The measure has enormous significance. It would literally change modern legislative processes to an enormous degree.

This country throughout most of its history had a small Government, small in terms of the portion of the GDP it consumed and small in terms of its regulatory impact. That has changed dramatically during this century. Prior to 1930, this Nation's government never exceeded 10 percent of the GDP, with two exceptions. Those exceptions were 1 year during the Civil War and 1 year during World War I. But outside of that, this Nation's tax burden and spending burden by the Federal, State, and local governments all combined never exceeded 10 percent of its GDP.

Since the 1930's, it has never been below 10 percent of the GDP. It has grown dramatically and now approaches 40 percent of the GDP, but the change isn't just in the dramatic increase in the portion of our GDP taken by government. The change is also in terms of who spends it. Originally, local and State governments spent by far the largest share of government expenditures, but since the 1930's that has reversed, with by far the largest share coming from the Federal Government.

The tax burden to support these dramatic increases in expenditures has grown on a consistent basis since the 1930's. Since 1980,

the Federal tax burden per capita has more than doubled and hardly a year has gone by where we haven't had a significant series of tax increases. Thus, on this 15th day of April, tax day, it is appropriate that we consider this issue and review the dramatic changes that our colleague from Arizona has proposed for us.

We are fortunate to have a very distinguished panel and I will ask our first witness, Congressman Jack Kemp, who is head of Empower America, to start us off.

PANEL CONSISTING OF JACK KEMP, CO-DIRECTOR, EMPOWER AMERICA, AND CHAIRMAN, NATIONAL COMMISSION ON ECONOMIC GROWTH AND TAX REFORM, WASHINGTON, DC; LLOYD N. CUTLER, WILMER, CUTLER AND PICKERING, WASHINGTON, DC; PETE DU PONT, POLICY CHAIRMAN, NATIONAL CENTER FOR POLICY ANALYSIS, AND MEMBER, NATIONAL COMMISSION ON ECONOMIC GROWTH AND TAX REFORM, WILMINGTON, DE; HON. DAVID SKAGGS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF COLORADO; AND HON. JOE BARTON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

STATEMENT OF JACK KEMP

Mr. KEMP. Well, Senator, thank you so very much for holding these hearings on a day on which most Americans are pretty much frustrated, depressed, and in many cases rather cynical about a system that was built over the years and which, as you alluded to in your opening comments, has been frustrating, cumbersome, and I would make a case today, Mr. Chairman, that it is causing a very severe dampening effect on the output, the productivity, the—excuse the expression—supply side of the economy.

It seems to me that if you look at the history of taxation, you can either approach it from the standpoint that all taxes raise revenue or taxes have a significant impact upon the behavioral instincts and incentives of people. I would make the case that it has both of those impacts. It does affect incentives and it obviously has to raise revenue.

There is no man or woman on this distinguished panel, there was no one on the Dole-Gingrich commission which I chaired—Governor du Pont was a very valuable and key member, holding hearings for over 6 months—there was no member of our panel that did not want to raise revenue in the most efficient and effective way without slowing down the ability of this economy to grow and without helping American families and American working men and women deal with the tax system of America.

We started out our hearings with the basic predicate that the purpose of taxation was to raise revenue, not to redistribute wealth. It was interesting to me, Mr. Chairman, that there are many bipartisan Members of the Congress—I am sitting here with Representative Skaggs, but you could find many Democrats, I am sure, including Dick Gephardt, who said as recently as a few weeks before our commission—I guess it was a couple months ago, now that I think about it—that once the 1986 tax law had been passed, it was not long before taxes were raised. The American people had some deductions taken out and rates were cut from 5 rates to 2

rates, 15 and 28. Within a very short period of time, sometimes rather circuitously, taxes began to climb.

The purpose of, as I understand it, the Kyl amendment—I can't speak for Senator Jon Kyl, of Arizona, a very good friend of mine, as are you, Mr. Chairman—and other cosponsors of this was to come up with a way of reforming the tax code and making it more difficult to raise taxes than to cut them. They seem to always go up; they very seldom go down.

Joe Barton in the House, among other men and women, has introduced this amendment in the House. I particularly believe it is a propitious time to tell the American people on this April 15 that the Congress is not going to do business as usual; that it is going to be more difficult to raise taxes than to cut them; that the purpose of taxation is not just revenue neutrality, albeit you could even argue with that over the short term.

President Kennedy, in 1962 and also in 1963, suggested that the purpose of cutting the tax rates was not to lose revenue. It was to prevent a recession. It was to raise the size—or increase, I should say, the size of the pie and to increase revenue.

I believe that Congress has backed itself into a corner, Mr. Chairman. In attempting to balance the budget, we have passed legislative amendments that would require revenue neutrality at the lowest and revenue increases at the highest as the purpose of public policy. In my opinion, the purpose or tax rates, again, should be to increase the size of the economic pie, increase the number of jobs, increase the climate for working and saving and investing and engaging in entrepreneurial activity in America.

I would make a case, Mr. Chairman, that this is necessary not only to tell Congress to stop—that is too harsh. It is not just Congress. It is OMB, the executive branch. It is many of our pundits, both on the left and right. I mentioned Dick Gephardt. Dick Gephardt, in testifying before our commission, said that once we get tax reform in place, it should be not impossible to change the rate, but it certainly should be difficult, and he suggested a national referendum.

To be frank, Mr. Chairman, I would be willing to go to the American people, the ultimate marketplace, for the purpose of raising a tax rate subsequent to reforming the code, which du Pont, Kemp and the National Commission on Economic Growth and Tax Reform suggested just a few months ago. We suggested one single tax rate and that it be low.

Pete and I have probably informally come to the conclusion that in peace time it ought not to be higher than 19 percent. It ought to be progressive for the poor. Low-income people should not pay at the same rate as so-called upper-income people, so we suggested a generous exemption for low-income people. We suggested that working men and women and families have a generous deduction beyond just that exemption.

We thought and believed and recommended that the payroll tax be deductible because, as you know, Mr. Chairman, the payroll tax, the FICA tax, is a huge burden on about 60 percent of working men and women and working families and low-income families in America. We have tried to offset it with an EITC, the Earned Income Tax Credit. Both du Pont and Kemp and Ed Fuelner and Ted

Forstmann and Shirley Peterson, a former commissioner of the IRS, among other men and women who served on our commission, suggested that once we get fundamental tax reform in place, like Dick Gephardt on the left of the aisle and those of us on the right of the aisle, it should be very difficult to change it.

I would suggest that a two-thirds majority, such as that required for overturning a veto by the President, would be a legitimate way of showing the American people that we are serious about tax policy in America. A lot of people will say it can't be done. It is already done, Mr. Chairman, at the State level. This is a great climate for recommending Federal policy that is in sync and inextricably tied to State policy.

Over 10 States have policies in which it requires a two-thirds supermajority to raise taxes. There are States that have, with empirical evidence, had higher levels of growth, more jobs created. In my opinion, it makes more sense to the average taxpayer in the country.

I would just close my informal remarks with the request that my full text be submitted for the record, A, and, B, to close on a point that both Pete du Pont, who has had very personal experience as Governor of Delaware, and Jack Kemp as the author of the Reagan tax cut of 1981 would also recognize empirical evidence.

There are two ways to raise revenues. You can either soak the taxpayer, hit the working man and woman, attempt in some cases to even soak the rich, albeit I would make the case that the rich never seem to get soaked. They always have ways of escaping taxation. It is the poor who get soaked. The incidence of taxation is always different than the burden.

While we place the incidence of taxation on production, output, work, savings, investment, and the supply side of the economy, the burden of taxation falls on the men and women who go without jobs, falls on the poor who can't get access to capital, falls on those people who are trying to work their way out of poverty. You cannot, in my opinion, Mr. Chairman, work your way out of poverty or work your way off welfare without two things, education and a job, and that ought to be at the forefront of the congressional mind's eye as we look at this constitutional amendment which simply would say raise revenue, but do it by expanding the size of the economy. Don't keep attempting to take it out of the hard-working men and women of America who not only want to work, but they want to save.

I will close with this thought. Yesterday, I had a friendly debate with one of your colleagues, John Breaux, of Louisiana, for whom I have high regard. He kept saying that the trouble with Kemp and du Pont and this issue is we favor the investor, the saver, the coupon-clipper, against the wage-earner.

I wanted to say then, and I didn't—I was on the CNN show with my friend, Jon Kyl, of Arizona, and I missed an opportunity, although I thought about it several times. I think the most fundamental mistake being made in America today is that somehow the wage-earner and the saver are different people. They are not different people. The wage-earner and the man and woman who want to save for a future, be it for medical care for their golden

years or education for their children, or whatever—they are the same people. It is just different stages of their lives.

We have got to stop this class warfare, Mr. Chairman—you have been a champion of that—and I can't think of a better way than passing the Kyl amendment and the Barton amendment in the U.S. House today, April 15, 1996.

Thank you.

[The information of Mr. Kemp follows:]

UNLEASHING THE AMERICAN SPIRIT

A GUIDE to Tax Freedom for Americans &
Spectacular Economic Growth for America!

Facts, Figures & Citizen Testimonies

How & Why America MUST Throw Out the Current Tax Code and Implement the Genuine Reform Proposed by
The National Commission on Economic Growth and Tax Reform,
Appointed by Senate Leader Bob Dole and Speaker of the House Newt Gingrich

with Introduction by
Jack Kemp
Commission Chairman

The Tax Test

Six Points of Principle

- **Economic** growth to expand opportunity and create jobs
- **Fairness** for all taxpayers
- **Simplicity,** so everyone can figure it out
- **Neutrality,** so people — not government make choices
- **Visibility,** so people know how much government costs
- **Stability,** so people can plan for the future

Six Points of Policy

- **A single tax rate**
- **A generous personal exemption** to remove the burden on those least able to pay
- **Lower tax rates** for America's families
- **Payroll tax deductibility** for working men and women
- **An end to biases** against work, saving, and investing
- **A 2/3 super-majority** in Congress required to raise the rate

Setting the Eagle Free

"An economy hampered with high tax rates will never produce enough revenue to balance the budget, just as it will never produce enough output and enough jobs."
— John F. Kennedy

Like Kennedy, President Ronald Reagan grasped the "paradoxical truth" that only lower tax rates could lead to higher growth. His leadership was my inspiration as we launched the tax reform movement in the early 1980s with the Kemp-Roth tax cut, paving the way for the greatest peacetime economic expansion the world has ever seen.

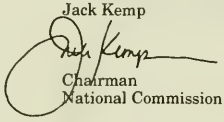
Never has this example had more urgency than today. America stands at the edge of extraordinary possibilities. The passing of the Cold War offers an opportunity to lead the world into an era of democratic capitalism, rising prosperity and technological progress. We must embrace this future — but we are being weighed down by our past: the built-up barnacles of counter-productive tax policies that punish risk-taking, penalize investment, and destroy the link between effort and reward.

American taxpayers have had enough. In election after election voters have sent the message that taxes are too high and government spends too much. The message of this commission is: hang on, we hear you, help is on the way! Senator Dole and Speaker Gingrich told us to begin with a blank slate and chart a totally new tax structure for America's next century. We held cross-country public hearings to hear *your* concerns — weighing the advice of ordinary taxpayers in reaching our final conclusions.

How do we make sure everyone pays their fair share? How do we ensure enough revenue to balance the budget and meet basic needs? Most importantly, how do we double the rate of economic growth, create opportunity, and get America growing again? This synopsis of our report attempts to offer some answers by laying the groundwork for tax reform that restores working Americans' control over their pocketbooks, their businesses, their destinies, their lives.

John Gardner has said of the ingredients of great nations: "There occurs at breathtaking moments in history an exhilarating burst of energy and motivation...and a severing of the bonds that normally hold in check the full release of human possibilities. A door is opened, and the caged eagle soars." That eagle, the symbol of our nation, represents the infinite possibilities awaiting the American people. Our mission, the intent of our recommendations, is to open that door and set the eagle free.

Jack Kemp



Chairman
National Commission on Economic Growth and Tax Reform

Repeal the Tax Code: Highlights of the Commission's Report

- The Commission believes the current tax code is **beyond repair**...complex, wasteful, economically destructive — enforced by a bureaucracy many see as too big, too powerful, too intrusive.
- The Commission recommends **that the current Internal Revenue Code be repealed in its entirety.**
- **Replace the system with a single low rate, taxing income only once with a generous personal exemption and full deductibility of the payroll tax for America's working men and women**.
- This system will **reduce the tax burden** for all Americans...while removing it entirely from the poor.
- The new system will be **set in stone:** with **a 2/3 super-majority vote of the Congress required to raise the tax rate**.
- These changes can help **double the rate of economic growth** — create jobs, raise family incomes, expand ownership, entrepreneurship, and opportunity.
- Only a system which promotes economic growth can produce the needed revenues to **balance the budget and reduce the burden of our national debt.**

What's Wrong With the System? 3 Major Problems We Must Solve Now

1. ***Economically Destructive*** — Steeply graduated rates on labor and capital destroy jobs, penalize saving and investment, and punish personal efforts to get ahead.
2. ***Impossibly Complex*** — Mindboggling complexity places a huge burden on taxpayers while draining precious resources from our economy. Tax rules are so confusing that even IRS agents have trouble figuring them out.
3. ***Overly Intrusive*** — vast IRS enforcement powers are increasingly seen as infringements on privacy and personal freedom. Too many Americans feel the IRS says they are "guilty until proven innocent" — and resent being treated as criminals.

The Road to Tax Tyranny

"When men get in the habit of helping themselves to the property of others, they cannot easily be cured of it." — 1909, New York Times editorial protesting the first income tax.

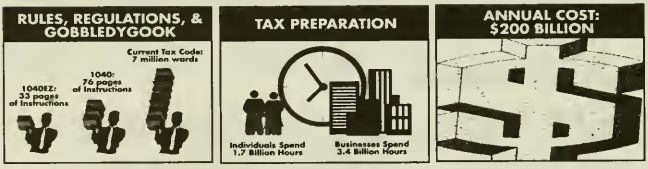
- The income tax was enacted in 1913 — and then, less than 2% of Americans were required to file. Rates ranged from 1 to 7% — the highest rate applying to those who made the equivalent of $7.7 million by today's standards.

- As America prepared to enter World War I the top rate soared to 67%. By World War II, **the top rate was 94%.**
- Throughout the 1950s the highest rate remained at more than 90%. John Kennedy cut that rate to 70%. Ronald Reagan cut it to 28%.
- Both tax cuts triggered unprecedented economic growth, new businesses and new jobs.
- Because of President Clinton's tax increases, today's rate is rising again — the top tax rate now hovers higher than 40%.

Complex, Confusing, Costly and Coercive

"The current tax structure is way out of date with the real world, too complicated with too many loopholes. [We] say dump it!" — Citizen's letter to The Commission

- The current tax code is *seven million* words (7,000,000). Lincoln's Gettysburg Address is 269 words; and the Declaration of Independence, 1,337 words.
- The IRS' "simplest" return, the EZForm 1040, has 33 pages of instructions. The IRS' Form 1040 has 76 pages of instructions.
- American business will spend 3.4 billion hours, and individuals will spend 1.7 billion hours, *simply trying to comply with the tax code.* That's equivalent to a "staff" of 3 million people working full time, year round, just on taxes.
- This costs our economy $200 billion each year — that's like taking every new car, van and truck General Motors builds in a year and dumping them into the ocean.
- Twice as big as the C.I.A. and five times the size of the F.B.I., the I.R.S. controls more information about individual Americans than any other agency.
- Without a search warrant, the I.R.S. can search personal financial records; without a trial, the I.R.S. can seize private property.
- Harvard economists estimate that average incomes in the U.S. could be 15-20% higher without the economic distortions caused by the tax code. That's as much as $6,000 per year for middle income families.



The Tax Test — A Checklist for Real Reform

The principles and recommendations contained in the report comprise "The Tax Test" — a blueprint that provides the foundations for legislative reform. We ask that Congress not pass nor the President sign any legislation that fails to meet this test.

I. *Economic Growth*: Because expanding prosperity and opportunity form the foundation of a free and healthy society.

- None of the challenges facing America — from poverty to crime to the budget deficit — can be solved without strong and continuing economic growth.
- And yet last year our economy grew at an anemic 2.1%! America cannot afford to limp into the 21st Century on such a feeble rate of economic growth.
- No nation in history has ever taxed its way into prosperity. Throughout the ages, lower taxes have meant higher economic growth, higher living standards and more jobs.
- Here at home we've had three periods of powerful economic growth:
  1. 1920s — After the Harding-Coolidge tax cuts, the economy grew at more than 5% per year.
  2. 1960s — After the Kennedy tax cuts, the economy grew at 5% while revenues rose 29% in 4 years.
  3. 1980s — Reagan tax cuts. From 1982-1989, 7 years of growth at nearly 4% annually. 21.5 million new jobs and over 4 million new businesses created.
- REMEMBER: Higher **tax** rates don't produce higher revenues — only higher **growth** rates do.

Tax rates have gone up, gone down, gone up again — but tax revenue as a *percentage* of national output has remained the same. Looking at the chart on the following page: government historically collects about 19% of the GDP — no matter how high the tax rate is pushed. Higher rates simply mean a smaller economy — and less income to tax. 19% of a booming economy brings in more revenue than 19% of a weak one — another reason why reform must spur economic growth.

II. *Fairness*: Because democracy is based on the principle of equality before the law.

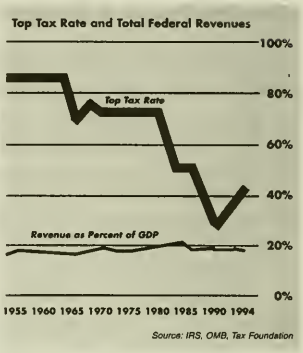
"...I do not mind paying my fair share...but I feel that many, many people and companies are not paying their fair share because they have the money to hire smart accountants and lawyers." — Christine W. Perkowski, PA., Letter to Commission

In order to restore fairness, a new system must:

Tax equally: One rate respects equality before the law.

- Eliminate tax "loopholes" — the exemptions, deductions and credits that traditionally benefit the rich.

- Don't punish success — by slapping higher rates on hard work, creativity and entrepreneurial risk taking.
- If a man earns ten times the income of another, he should pay ten times as much taxes — no more, no less.



Tax progressively: A compassionate system must lighten the load on those least able to pay.

- Americans must be able to feed, clothe and house their families before they're asked to feed the federal spending machine.
- Today, the highest marginal tax rates in America are paid by those who are trying to move from welfare to work. When lost benefits are included, this effective rate can reach 100%.
- A generous exemption can provide individuals with an "economic head start" — letting them start to climb the ladder of opportunity before taxes take effect.

Lower tax rates: The rate must be low and kept low.

- Taxpayers are unanimous: taxes are too high, and government spends too much.
- By lowering taxes and restraining spending, we can restore the balance of power between the federal government and the citizens who pay its bills.

III. *Simplicity*: Because life is too short and peace of mind too precious to waste your time and lose your temper trying to figure your taxes.

- The tax code grows in complexity every year — making it increasingly impossible for average taxpayers to understand.
- A simplified, single rate system will let taxpayers file their return on one sheet of paper in less time than it takes to complete the morning crossword puzzle.

IV. *Neutrality*: Because the code shouldn't pick winners or losers, but let people make decisions based on their own needs and dreams.

- The purpose of taxes is to raise the revenue needed to run government — period.
- This should be done in a way that does the least possible damage to the economy.
- The most damaging aspect of today's code is the double and triple taxation of saving and investment.

V. *Visibility*: Because those who pay for government have a right to see the bill.

- Hidden taxes further the fantasy that government is free, leading many to "consume" more government than they otherwise would.

- A visible tax rate gives citizens an honest accounting of government's expense.
- By keeping the tax rate in plain view — we can make it harder for politicians to raise taxes without our consent.

VI. *Stability*: Because taxpayers should be able to plan for their future without the rules getting changed mid-game.

- Over the past 40 years, the tax code has had 31 "significant" reforms and more than 400 revisions through public law.
- These changes have created a climate of confusion and uncertainty.
- A stable tax code must let individuals start a business, buy a house or take out a loan without fear of constant changes in the tax code.

A New Tax Code For The 21st Century
Key Recommendations

- Adopt a single, low tax rate with a generous personal exemption
- Lower the tax burden on America's working families and remove it from those least able to pay
- End biases against work, saving, and investment
- Allow full deductibility of the payroll tax for working men and women
- Require a two-thirds super-majority vote in Congress to increase the tax rate

Discussion

One Rate

One tax rate, combined with a generous personal exemption, produces a progressive average tax rate. Low-income taxpayers pay little or no tax — but above the threshold, everyone faces the same rate on additional income.

Lower the Tax Burden for All

The single rate should be *as low as possible* — and lowered over time as a growing economy yields higher revenues. Any extra revenue should be seen as a "growth dividend" to be paid out to the American people.

End Biases Against Work, Saving and Investment

Multiple taxation goes against the grain of basic American values — such as thrift, hard work, and entrepreneurial risk-taking. These biases must end — including elimination of the tax on capital gains.

- At 28% — America's capital gains tax rate is one of the highest of any developed nation. It's not fair for America's workers and entrepreneurs to compete against nations with lower rates: France, 16%; Japan, 1%; Germany, South Korea, Hong Kong, 0%.
- By punishing risk-taking and shrinking the pool of seed capital — the capital gains tax destroys jobs and kills businesses before they have a chance to be born. Those hit hardest are not the wealthy, but those who have yet to realize their capital gains: the poor, the young, and minorities.

Eliminate "Death Taxes"

It makes little sense and is patently unfair to impose extra taxes on people who choose to pass their assets to their children or grandchildren. Families faced with these confiscatory taxes often are forced to sell off farms or businesses, destroying jobs in the process.

Full Deductibility of Payroll Taxes for All Working Americans

Many employees pay more in payroll taxes than in federal income taxes. When employer/employee payroll taxes of 15.3% are taken into account, a worker in the 28% tax bracket faces a brutal marginal rate of 43% on any additional income earned.

Making the payroll tax deductible means income taxes would be calculated on working families' real net incomes.

Simplify International Taxation

The current international taxation system is one of the biggest headaches for American businesses — damaging our competitiveness abroad, while encouraging businesses to reinvest profits overseas rather than bringing them home.

A new system must be clearer and simpler. It must not work to discourage investment in research and development in the U.S.

Strengthen Private Retirement Savings

Americans are not saving enough for their own retirement.

Even under a new tax system, there is no guarantee that all individuals or families will save enough to be secure in their retirement. Without sufficient retirement saving, many people will become dependent upon government in their old age, necessitating either sharp increases in taxes on future generations or a significantly diminished standard of living.

Therefore, any new tax system should encourage people to save for their own retirement.

Two-Thirds Super-Majority Vote to Raise the Tax Rate

The roller-coaster ride of tax reform in past decades has fed citizens' cynicism about the possibility of real, long-term reform. By safeguarding these changes with a two-thirds super-majority vote, we can rebuild Americans' trust in the system.

Deductions and Exemptions

The home mortgage interest deduction has spurred home ownership in America; an important goal of The Commission is to spread ownership to give more people a stake in the system.

And, at a time when America needs a renaissance of private giving and commitment to overcome those social problems which government programs have either failed to improve or made worse — we need a system which encourages people to take more responsibility for communities and neighbors in need.

America should debate the best way to protect these institutions and preserve the values they represent within the context of the dynamic new tax system The Commission envisions.

Conclusion

It is said that every breakthrough in human understanding has come in the form of a simplification. The complex, bureaucratic tax code of the 20th century will not help us keep pace with the challenges of the 21st.

The rewards of the 21st century tax code outlined in these pages go beyond the obvious simplicity and freedom a single-rate would afford. The impact on the economy would be immediate and profound: doubling our economic growth rate over the course of the next decade. The moment the dead weight and distortions of the current system are lifted, the explosion of new businesses and new jobs would transform the economic and social landscape of the country.

By freeing citizens from the costly encumbrances of the current tax code, by strengthening the link between effort and reward, by allowing individuals to keep more of what they earn, and by freeing the pent-up power of our economy, this new system can lead to Lincoln's "new birth of freedom" and launch us into the next American century.

Members of The National Commission on Economic Growth and Tax Reform

Chairman: **Jack Kemp**, Co-Director of Empower America. Former Secretary, The U.S. Department of Housing and Urban Development. Nine terms in U.S. House of Representatives from Buffalo, NY area. Played professional football for 13 years as quarterback for the San Diego Chargers and Buffalo Bills.

Vice Chairman: **Edwin J. Feulner, Jr.**, president of The Heritage Foundation, a Washington-based public policy group. Chairman of the Institute for European Defense and Strategic Studies in London.

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If you support the goals of this summary, you will want to read the complete Report of The National Commission on Economic Growth and Tax Reform.
Contact The Commission at:

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Senator BROWN. Thank you. Senator Simon wanted me to convey his thanks along with mine for this distinguished panel coming to testify today. He is en route, and I would ask unanimous consent that the statement of Governor Wilson be entered in the record at this point, without objection.

[The prepared statement of Governor Wilson follows:]

PREPARED STATEMENT OF HON. PETE WILSON, GOVERNOR OF CALIFORNIA

Mr. Chairman, thank you for the opportunity to provide testimony today in support of Senate Joint Resolution 49, commonly referred to as the Tax Limitation Amendment.

I would like to commend the chairman for holding this hearing today on a very important issue, as well as Senator Kyl, the sponsor of the amendment. I would extend similar recognition to the House of Representatives, where a vote on the amendment will occur this afternoon.

From personal experience, I am convinced that requiring supermajorities to approve tax increases will be a useful and effective tool in reigning in government spending. In the face of persistent budget deficits, this is the best hope for protecting taxpayers from political leaders whose tax-and-spend propensities cannot otherwise be checked.

The committee is scheduled to hear from a number of witnesses who will discuss this amendment in its overall federal fiscal context. For this reason, I will direct my initial comments toward comparing the amendment with a similar supermajority requirement in the California state budget process.

In California in the early 1990s, the state suffered by far the longest, deepest economic recession since the Great Depression. Three quarters of a million Californians lost their jobs, producing both a sharply increased demand for public assistance and plunging state revenues. Over the first quarter of calendar '91, the state suffered a chasmic revenue gap amounting to more than $14 billion, roughly one-third of the state's General Fund.

To face this problem responsibly, I proposed a budget to bring spending in line with expected revenues. But after agreeing to over $7 billion in spending cuts, heavy Democratic majorities in both houses of the State Legislature balked at further cuts and insisted the balance of the revenue gap be filled by temporary tax increases to avoid even deeper reductions in many programs. After protracted negotiations, agreement was eventually reached on a budget that both cut spending and raised taxes. A half-cent sales tax increase and the addition of two top personal income tax brackets were temporary and have since expired.

The tax increases were painful, and the wrong choice for a state already in great need of making its business environment more competitive for investment and job creation. But they were the price demanded by the Democratic majority for the structural changes that allowed us to lock in guaranteed spending cuts—long overdue changes and long over-due cuts in entitlement spending necessary to ensure the state's long-term fiscal health. Over a 20-year period, California's automatic annual cost-of-living adjustments in the cash grant paid to welfare recipients has increased from twenty-sixth in the nation to second highest. In May 1990, the Commission on State Finance projected that the state's general fund budget would reach $64 billion in Fiscal Year 95-96. But because of the cuts we've made, it is now only two-thirds of that amount.

The state's requirement for a two-thirds vote to approve the budget and to increase taxes was fundamental to securing these essential spending cuts. Without the two-thirds vote requirement, the Democratic majorities could and would have balanced the budget with much greater tax increases, without making the deep spending cuts I required of them, and a different governor might have signed such a budget.

But as a result of California's 1991–92 budget agreement, the state has been used by some as an example that even supermajority requirements cannot entirely foreclose the possibility of tax increases. While that's true, the supermajority requirement makes it enormously more difficult to raise taxes. And I would underscore the critical difference between the California and the federal budget process. In California, a two-thirds majority is required to pass the budget, as well as to pass a tax increase. In contrast, the Tax Limitation Amendment requires a supermajority only for a revenue increase. Thus, a majority can cut spending by passing a reconciliation measure relying solely on spending controls, but a liberal majority could not pass a tax increase with a simple majority. This would provide a significantly increased incentive for Congress and the President to meet budget targets without turning to

tax increases. Given the current tax burden on Americans, such an incentive to control spending is exactly what the budget process needs.

Mr. Chairman, the Tax Reform Act of 1986 was an arduous undertaking pursued by President Reagan and the Congress in hopes of making the tax code flatter and fairer. No small amount of effort was expended in an attempt to lower tax rates and broaden the tax base. Unfortunately, those successes have been gradually eroding. The first slip came in 1990, when an additional tax bracket was added to the Internal Revenue Code as the Democrat's price for promises to cut federal spending—promises that sadly never materialized. Then, in 1993, America was hit by President Clinton's $255 billion tax increase to supposedly balance the budget. That commitment too was subsequently abandoned in 1995, and has since been resurrected in a number of very questionable forms.

Weaving the promise of the Tax Limitation Amendment into the fabric on the Constitution is an effort to restore the faith of the American people—who have good reason to be jaded. In 1992, candidate Bill Clinton promised middle-class families a tax cut. Instead, their taxes went up The President has now admitted of course that his 1993 tax increase was a "mistake." But it is well worth noting that the 1993 budget was approved by a single vote in both the House and the Senate—and then only through strenuous White House arm twisting. Had a supermajority been required to approve tax increases at that time, the Congress could have well saved the President from himself.

At the same time, the President's recent veto of the Balanced Budget Act shows just how hard it can be to cut taxes, owing to the constitutional protections afforded the status quo. The Republicans' $500-per-child tax credit alone would have benefitted more that three million California families, and nearly one-half million middle-class taxpayers in my state would have seen their income taxes drop to zero. But the President, preferring more federal spending over an honest, balanced budget, decided Washington could better spend the $245 billion that Congress had earmarked for the people. It is very hard indeed to wrench money and power from Washington. However, it should be even harder to raise taxes any higher than they currently stand.

Americans are not undertaxed. In survey after survey respondents place the ideal cumulative rate of federal, state, and local taxes at roughly 25 percent. Yet the taxes of most middle-class taxpayers routinely exceed this rate, and many taxpayers face marginal rates in excess of 50 percent. The Tax Limitation Amendment says "enough is enough." By establishing a strong constitutional disincentive to pursuing ever higher taxes, it can be ensured that the 1993 Clinton budget will be the high water mark of American taxation.

As demonstrated in California, controlling spending is the only responsible path to fiscal health, and the only sound way to wean the federal government from continued deficit spending. The line-item veto, finally passed thanks to the new Republican Congress, is a positive step in reforming the budget process to help produce better budgets. But as Congressional Republicans have argued time and again, entitlement programs must be reformed to close the structural budget deficit, and discretionary spending must be judiciously scrutinized. The Tax Limitation Amendment provides an additional incentive in the budget process to do just these things, rather than to repeatedly turn to new tax increases.

The Tax Limitation Amendment restores a fundamental tenet held by those who framed the Constitution and the Bill of Rights. Namely, that in the face of serious controversy or doubt, the government must ere on the side of freedom—in this case, freedom from an ever-increasing tax burden.

History has clearly and repeatedly shown that as governments grow, they grow more intrusive. The clearest and most painfully relevant example is provided by this century's increase in the size and intrusiveness of the federal bureaucracy—as more and more federal employees have required more and more revenue to mind the business of American taxpayers.

The participants in the Boston Tea Party knew there was a relationship between taxation and freedom. They, however, mistakenly assumed that elected representation would provide relief. We now know that at times we need to be protected from our representatives.

A supermajority will go a very long way toward providing needed protection against tax increases and the growth in government and government intrusiveness which they finance.

I wholeheartedly endorse the Tax Limitation Amendment.

Thank you.

Senator BROWN. Senator Kyl, this takes it a little out of order, but since we are addressing your amendments, I would like you to go ahead with our opening statement now, if you would be willing.

STATEMENT OF HON. JON KYL, A U.S. SENATOR FROM THE STATE OF ARIZONA

Senator KYL. Well, Mr. Chairman, I appreciate that. In view of the fact that we have this distinguished panel before us, I will ask unanimous consent to submit my statement for the record and simply extract a few thoughts from it, if I might.

I would also note that the case really was made by Secretary Kemp. In fact, my sponsorship of this particular amendment was a result of the recommendations of the so-called Kemp Commission. The Commission noted that if we were successful in developing a flat tax or single tax rate, whether it be on sales or on income, that eliminating most of the deductions and exemptions and credits would create a severe vulnerability for all taxpayers unless a supermajority was required for Congress to raise that rate.

I would also note that the States that have a supermajority requirement have enjoyed singular success both at keeping taxes down. States that have a supermajority to raise taxes in their own State constitutions have reduced taxes by 2 percent, while those States that do not raise taxes by 2 percent, and spending is also affected. As a matter of fact, spending in the States without this supermajority requirement has gone up by 9 percent. It has only gone up 2 percent in the States with the requirement.

I was asked this morning by a radio person what our Founding Fathers would have said about a supermajority to raise taxes. Of course, a supermajority exists in 10 different places in the Constitution, in each of those places where the Founding Fathers thought it was important to develop a strong consensus before action were to be taken.

For example, to override a Presidential veto obviously should require more than a simple majority. That should really represent a strong consensus, and I suspect—and I reflected on this this morning—that if our Founding Fathers were to look at the Federal Government today, the degree to which it burdens its citizens by over-regulation and over-taxation and too much spending, it wouldn't take them long at all to agree that this is another area in which a supermajority requirement should exist; that is to say that it should require a two-thirds vote to raise taxes.

If you look at a couple of the charts we have there—and if I could ask one of my staff people to stand next to the chart—you note that in the family budget, and that is what this all boils down to here, that Federal, State, and local taxes consume more of the family budget than food, shelter, and clothing combined. It illustrates the fact that almost 40 percent of the personal income today is paid in Federal, State, and local taxes, whereas—well, I don't know the State number, but in the Federal tax number, in 1950, for example, it was 3 percent of income and today it is 25 percent of income. Clearly, it has been too easy to raise taxes.

Just a couple of other charts that I wanted to refer to, Mr. Chairman. This chart shows the Federal tax burden per capita. This is the amount that individuals are being taxed, and you can see the

same dramatic increase in aggregate terms. You can see that it has been too easy to raise taxes. That is why we need a two-thirds majority in the House and Senate to raise taxes so that it won't be so easy.

This next chart—as the economists would call it—is the macro. Since 1950, you can see how Federal taxes have dramatically risen in gross numbers. It is obviously too easy to raise taxes—another illustration of why we need the two-thirds vote.

Just two final points, Mr. Chairman. I can understand now why T.S. Eliot called April the cruelest month of all because this is the month where we all have to focus on the impact of taxes. But there is another side of this that we frequently forget and that is the amount of time and effort and talent that it takes to complete our tax paperwork.

One of the other recommendations of the Kemp Commission, of course, was to simplify the tax code so that we didn't have this tremendous loss. According to the IRS itself, individuals have spent about 1.7 billion hours on tax-related paperwork for their filings today. Businesses will have spent another 3.4 billion hours. The Tax Foundation estimates that the cost of compliance will approach $200 billion. So it is not just the cost of the taxes themselves, but the waste to the economy as a result of this extraordinary burden.

Mr. Chairman, as I said, I will put my full statement in the record. I think that Secretary Kemp has made the argument for the two-thirds requirement and anything I add would be, to put it charitably frosting on the cake.

[The prepared statement of Senator Kyl follows:]

PREPARED STATEMENT OF SENATOR JON KYL

By midnight tonight, millions of Americans will have filed their income tax returns. According to estimates by the Internal Revenue Service, individuals will have spent about 1.7 billion hours on tax-related paperwork. Businesses will have spent another 3.4 billion hours. The Tax Foundation estimates that the cost of compliance will approach $200 billion.

If that is not evidence that our Tax Code is one of the most inefficient and wasteful ever created, I do not know what is. Money and effort that could have been put to productive use solving problems in our communities, putting Americans to work, putting food on the table, or investing in the nation's future are instead devoted to convoluted paperwork.

It is no wonder that the American people are frustrated and angry, and that they are demanding radical change in the way their government taxes and spends.

There are a number of proposals for comprehensive tax reform that will be debated during the next year. Senator Richard Shelby and House Majority Leader Dick Armey have proposed a flat tax. Versions of the flat tax have also been suggested by Steve Forbes and Senator Phil Gramm. The Chairman of the Ways and Means Committee has recommended that the income tax be pulled out by its roots and replaced with a national sales tax. Senator Richard Lugar has proposed a sales tax, as well.

Today's hearing is intended to focus, though, on a change that should be made whether we move to a flat tax or sales tax or some alternative. Indeed, it is a change that should be made whether comprehensive tax reform succeeds or not. I am talking about a change that would require a two-thirds majority vote of the House and Senate to approve tax increases. The House of Representatives is scheduled to vote on the proposal, the Tax Limitation Amendment, later today.

The Tax Limitation Amendment, which I introduced in the Senate with the support of 20 other Senators, would require a two-thirds majority vote of each house of Congress for the approval of tax increases. The two-thirds supermajority that many of us believe should be added to the U.S. Constitution was recommended by the National Commission on Economic Growth and Tax Reform, appointed by Senate Majority Leader Dole and Speaker Gingrich. The Commission, chaired by former

HUD Secretary Jack Kemp, who is scheduled to testify before our panel today, advocated a supermajority requirement in its recent report on how to achieve a simpler, single-rate tax to replace the existing maze of tax rates, deductions, exemptions, and credits that makes up the federal income tax as we know it today.

Here are the words of the Commission:

> The roller-coaster ride of tax policy in the past few decades has fed citizens' cynicism about the possibility of real, long-term reform, while fueling frustration with Washington. The initial optimism inspired by the low rates of the 1986 Tax Reform Act soured into disillusionment and anger when taxes subsequently were hiked two times in less than seven years. The commission believes that a two thirds super-majority vote of Congress will earn Americans' confidence in the longevity, predictability, and stability of any new tax system.

In the 10 years since the last attempt at comprehensive tax reform, Congress and the President have made some 4,000 amendments to the Tax Code. Four thousand amendments. Without the protection of the Tax Limitation Amendment, taxpayers would be particularly vulnerable to tax rate increases, particularly if tax reform eliminates many of the tax deductions, exemptions, and credits in which they find refuge today.

The Tax Limitation Amendment will make it more difficult for Congress to raise taxes. It will also help restore confidence, stability, and predictability to the Tax Code.

Ideally, the Tax Limitation Amendment should be put into place after comprehensive tax reform is accomplished. That is because tax reform necessarily aims to broaden the tax base—eliminating the maze of tax deductions, exemptions, and credits that make up the income tax as we know it today—and then apply one low tax rate to whatever amount of income is left. Because base-broadening would be subject to a two-thirds majority vote under the amendment, some are concerned that it could make comprehensive tax reform more difficult to achieve.

I would note that the Tax Reform Act of 1986 would have met the two-thirds test. The tax reform bill passed the Senate by a vote of 74 to 23, well over the 67 votes that would be required had the Tax Limitation Amendment been in place at that time. The House passed the bill by a vote of 292 to 136, two votes more than would have been required under the supermajority amendment.

So tax reform is not necessarily a reason to oppose the Tax Limitation Amendment at this time. Moreover, it is important to begin the debate now on the proposed constitutional amendment, because it takes a long time to build the necessary support in Congress and to win ratification by the states.

Another criticism comes from those who believe that tax increases should remain readily available to Congress as a tool of fiscal policy.

I want to make just a few points in response to that criticism. First, the Tax Limitation Amendment itself cuts no taxes; it only raises the bar on future tax increases. Many people, myself included, believe that taxes are already far too high. This amendment, in effect, says, "enough is enough." It makes Congress find a way to meet its obligations without taking more from the pockets of the American people.

Understand that the average family already pays more in taxes than it does on food, clothing, and shelter combined. According to the Tax Foundation, federal taxes amount to about 27 percent of the family's budget, and state and local taxes consume another 12 percent—for a total of 39 percent. But spending on food, clothing, and shelter totals only about 28 percent of the family budget. And families still have to find a way to pay for everything else they need—for example, medical care, transportation, education, and an occasional vacation or dinner out—out of the meager amount that is left.

So what the Tax Limitation Amendment says is that government already takes far too much from hard-working Americans and should take no more, unless there is a very broad and bipartisan consensus in Congress and around the country.

A second point. There is no small irony in the fact that it will take a two-thirds majority vote of the House and Senate to overcome President Clinton's veto and enact the Balanced Budget Act with its tax relief provisions. By contrast, the President's record-setting tax increase in 1993 was enacted with only a simple majority—and not even a majority of elected Senators, at that. Vice President Gore broke a tie vote of 50 to 50 to secure passage of the tax-increase bill in the Senate.

The Tax Limitation Amendment is based upon a simple premise—that it ought to be at least as hard to raise people's taxes as it is to cut them. What we are attempting to do with this amendment is force members of Congress to think of tax increases, not as a first resort, but as a last resort.

A third point. The amendment will make it harder to raise taxes, to be sure. But perhaps even more important than that, it will force Congress to fundamentally reassess the way it goes about raising revenue. Remember, the amendment does not limit revenue to the Treasury; it merely precludes tax rate increases without a two-thirds majority vote.

Most of us would agree that lower tax rates stimulate the economy, resulting in more taxable income, more taxable transactions, and more revenue to the Treasury. The tax cuts of the early 1980s are a case in point. They spawned the longest peacetime economic expansion in our nation's history. Revenues to the Treasury increased as a result—from $599.3 billion in FY81 to $990.7 billion in FY89, up about 65 percent.

High tax rates, on the other hand, discourage work, production, savings, and investment, so there is ultimately less economic activity to tax. That is precisely what Martin Feldstein, the former chairman of the President's Council of Economic Advisors, found when he looked at the effect of President Clinton's 1993 tax increase. He found that taxpayers responded to the sharply higher marginal tax rates imposed by the Clinton tax bill by reducing their taxable incomes by nearly $25 billion. They did that by saving less, investing less, and creating fewer jobs. The economy eventually paid the price in terms of slower growth.

It is interesting to note that revenues as a percentage of Gross Domestic Product (GDP) have actually fluctuated around a relatively narrow band—18 percent to 20 percent of GDP—for the last 40 years. Revenues amounted to about 19 percent of GDP when the top marginal income tax rate was in the 90 percent range in the 1950s. They amounted to just under 19 percent when the top marginal rate was in the 28 percent range in the 1980s. Why the consistency? Because tax rate changes have a greater effect on how well or how poorly the economy performs than on the amount of revenues that flows to the Treasury relative to GDP.

In other words, how Congress taxes is more important than how much it can tax. The key is whether tax policy foster economic growth and opportunity, measured in terms of GDP, or results in a smaller and weaker economy. Nineteen percent of a larger GDP represents more revenue to the Treasury and is, therefore, preferable to 19 percent of a smaller GDP.

Requiring a supermajority vote for tax increases is not a new idea. It is an idea that has already been tested in a dozen states across the country. In 1992, an overwhelming majority of voters in my home state of Arizona—72 percent—approved an amendment to the state's constitution requiring a two-thirds majority vote for tax increases.

There is a reason that the idea has been so popular in Arizona and other states. Tax limits work. According to a 1994 study by the Cato Institute, a family of four in states with tax and expenditure limits faced a state tax burden that was $650 lower, on average, five years after implementation than it would have been if state tax growth had not been slowed.

The Tax Limitation Amendment will force Congress to be smarter above how it raises revenue. It will force Congress to look to economic growth to raise revenue, instead of simply increasing tax rates. It will protect taxpayers from additional tax increases.

I look forward to hearing from the witnesses who will come before the Subcommittee today on this important initiative.

Senator KYL. I would also like to submit for the record statements in support of the Tax Limitation Amendment by the Governor of the State of Virginia, the Hon. George Allen, who could not be here today; the Governor of the State of Massachusetts, the Hon. William Weld; Lowell Gallaway, Department of Economics of Ohio State University; and a statement by Senator Rod Grams, of Minnesota, who was planning to be here but could not be here today as well.

Mr. Chairman, I thank you for the opportunity to make this brief statement.

Senator BROWN. Without objection, the statements will be entered in the record.

[The prepared statements of Governor Allen, Governor Weld, Mr. Gallaway, and Senator Grams follow:]

PREPARED STATEMENT OF GOVERNOR GEORGE ALLEN, GOVERNOR OF VIRGINIA

Mr. Chairman and members of the Committee, good morning. While I regret that I am unable to join you personally today, let me commend you for holding this important hearing on a measure I believe would help restore accountability and force a much-needed discipline on the federal government; a constitutional amendment to require a two-thirds vote to increase taxes.

Indeed, my good friend, Senator Jon Kyl of Arizona, and I worked hard to pass a balanced budget constitutional amendment with a similar tax-limitation provision during the 102nd Congress when we were members of the U.S. House of Representatives. Unfortunately, the guardians of the "big government" status quo prevailed. Let's not allow that to happen this time.

Americans today are paying the highest percentage of their incomes in taxes in the history of the United States. In 1948, the average American family with children paid only 3% of its income to Uncle Sam. Today, the same family pays 24.5%. In Virginia, average taxpayers will work this year until April 29th just to pay their taxes.

Opponents of this measure proceed from the assumption that the taxpayers' money first belongs to government; that the government should collect through taxes as much as the people will permit; and that it's the governments' job to redistribute the taxpayers' money in ways politicians and bureaucrats think best. I believe taxpayers' money belongs to the people who earned and produced it. The American people know better than any government official how best to use their hard earned money.

Mr. Chairman, I hope that Congress will adopt this common sense initiative and send it to the States and to the people for our ratification as quickly as possible. If we are diligent and determined in our attempts to bring discipline and accountability back to government, we can begin to fulfill our duties as responsible public servants. For a change, let's do not what is convenient for government. Let's do what is right for the American taxpayers.

THE COMMONWEALTH OF MASSACHUSETTS,
Boston, MA, April 15, 1996.

Hon. JON KYL,
U.S. Senate, Washington, DC.

DEAR SEANTOR KYL: I am writing to commend you for sponsoring a resolution that proposes a constitutional amendment to require a two-thirds majority vote in each house to approve tax rate increases.

The current federal, system is weighted in favor of higher and higher taxes. Special interest groups and their lobbyists, who work hard to protect specific spending programs, have tended to prevail over the American people's strong desire to keep more of their own money. The result has been exponential growth in the size of the federal government, higher and higher taxes, and deeper and deeper deficits. The system is out of balance in a way never envisioned by the Founding Fathers. We need to provide our citizens with a strong constitutional tool to protect them from legislative bodies which have shown an insatiable desire to tax and spend in order to perpetuate incumbency.

I want to give you my assurances that if Congress passes this resolution, I will do everything in my power to see that the Massachusetts Legislature becomes one of the first states to ratify it.

Sincerely,

WILLIAM F. WELD.

PREPARED STATEMENT OF LOWELL GALLAWAY, EDWIN L. AND RUTH E. KENNEDY DISTINGUISHED PROFESSOR OF ECONOMICS, DEPARTMENT OF ECONOMICS, OHIO UNIVERSITY

WHY WE NEED A SUPERMAJORITY

Whenever it is suggested that a super-majority be required in a vote to increase taxes, the cry goes up that it is undemocratic, that a vote on taxes should be treated just as any other legislative action, that a supermajority requirement violates the principle of majority rule. How valid is such an argument? Should taxes be simply one issue among many that our elected representatives must consider in carrying out their duties? For a variety of reasons, I think that the undemocratic argument is invalid and that taxes should be treated as something quite different.

First, it needs to be recognized that the taxing authority is a powerful one. Taxation of all by means of a simple majority vote offers a strong temptation for a tyrannical majority to confiscate the income and wealth of a minority. This was recognized rather early on in the life of the United States.

In 1819, Chief Justice of the Supreme Court, John Marshall, in *McCulloch* v. *Maryland,* offered the view that "the power to tax involves the power to destroy." Much has changed since 1819, mostly in the direction of confirming Marshall's worst fears. Marshall was not unique. Well before *McCulloch* v. *Maryland,* the inherent dangers of taxation were recognized. The Scottish historian Alexander Tyler remarked to the effect that democracy will only survive until a part of society discovers it can vote itself largesse out of the public treasury.

These remarks suggest the basic nature of the problem of taxes. Tax revenues are an invitation to government to spend the public monies. Richard Vedder, Christopher Frenze, and I have demonstrated that the tendency for Federal Government spending to escalate in the wake of taxation has grown systematically since the founding of the Republic until, in the post-World War II era, on average, an additional dollar of tax revenues has produced additional spending amounting to $1.59.[1] This phenomenon has led to the coining of a special term to describe it—tax-and-spend.

The repercussions of the operation of the tax-and-spend process on the American economy have been profound. Since 1948, it has led to almost a doubling of the proportion of Gross Domestic product that is claimed by the Federal Government in order to finance its activities. Recent research by Richard Vedder and myself reveals that current federal spending is at a level that has negative effects on the volume of goods and service produced in the American economy. This is reported in a series of studies we are doing for the Joint Economic Committee of Congress describing the effects of increasing spending in the private sector of the economy by $1.38. The details of this analysis are described in the study appended to this statement, entitled, *The Impact of the Welfare State on the American Economy.*

How is it that we have created that state of affairs? The answer is simple. "Growing" the Federal Government in the post-World War II period has been just too easy, especially following the budget reforms of 1974. Moving to five-year budgeting cycles opened the door to fiscal mischief, at first by making it terribly difficult in the early 1980s to adjust downward spending baselines predicated on expected levels of inflation that were at least twice what actually occurred and, then, in response to the budget deficits this created, by affording the Congress an opportunity to play the ultimate "bait-and-switch" game. Increase taxes now and promise spending cuts in the so-called "out years" of the budget, "out-years" that just never seem to come.

I believe that if it had been more difficult to raise taxes, the parody that has become the budgeting process would have been far less likely to occur, levels of Federal Government spending would have been significantly less than presently observed, and we would not today be faced with the problem of dealing with an oversized Federal Government that is exerting a substantial "drag" on the American economy. How substantial? The rates of economic growth we have now become accustomed to, 2.4–2.5 percent a year as far as the eye can see, and significantly less than the long-term historic rate of 3.6 percent a year that was characteristic of the American economy for a quarter of a millennium prior to the growth slowdown than began in the 1970s. The implications of this difference are profound for a young person just beginning their income earnings years. Over the sixty year period that might be a typical life-expectancy for such a person, the difference between current growth rates and historic growth rates means a standard of living one-half of what it could have been at the end of their lifetime. We owe it to our children and grandchildren to arrest the economic cancer known as big government that eats at our substance. An important step in this direction would be to modify our constitutional arrangements to make it more difficult for our elected representatives to increase taxes. In this way, we can limit the potential for the tax-and-spend mentality to contribute to maintaining "big government" as we have come to know it.

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[1] Richard Vedder, Lowell Gallaway, and Christopher Frenze, *Taxes and Deficits: New Evidence ("The $1.59 Study"),* Joint Economic Committee, October 30, 1991.

The Impact of the Welfare State on the American Economy

Prepared at the request of

Representative Jim Saxton
Vice-Chairman
Joint Economic Committee

and

Representative Dick Armey
Majority Leader
U.S. House of Representatives

by

Lowell Gallaway and Richard Vedder

Ohio University
Athens, Ohio
45701

December 1995

The Impact of the Welfare State on the American Economy

Executive Summary

In recent decades many of the most important policy issues have revolved around the level and composition of federal spending. There is broad agreement that up to a certain point government functions enhance economic well-being, while after this point the burdens of excessive government spending can reduce economic growth relative to what it would otherwise be. Much of the debate over budget policy is over this question of where total government spending, or the spending level of a particular program, becomes counterproductive.

This study by two distinguished economists, Professors Lowell Gallaway and Richard Vedder of Ohio University, examines the issue of the optimal size of the federal government, expressed as a share of the economy, using econometric techniques. These two academic economists also estimate the net economic costs borne by the economy by the last dollar of federal spending. These additional economic costs are often referred to as a deadweight loss, a net reduction in output caused by excessive levels of federal spending.

Among the findings and implications of the Gallaway and Vedder study are:

⇒ The optimal level of federal government spending is about 17.6 percent of GDP. Beyond this point, the resources consumed by government impose more costs on the economy than benefits.

⇒ The current level of federal outlays is about 4 percentage points of GDP higher than its optimal level. Under the Republican policy of restraining deficit spending, the reduction in the GDP share of federal spending would substantially boost economic growth.

⇒ For every $1 dollar of federal spending growth curtailed, the private sector of the economy will expand $1.38 in the same year. In other words, every dollar of federal spending growth restraint produces a net economic benefit of 38 cents. On the other hand, the failure to constrain each $1 dollar increase in federal spending will cause a net reduction in economic growth of 38 cents.

⇒ Over seven years, economic output would be $2.45 larger for every dollar of spending restraint enacted in the first year and sustained through the period.

⇒ This study has important implications for the current policy debate. In any given year, for every $100 billion of projected federal spending growth curtailed, the economy would grow by an additional $38 billion. This increase in economic output continues into following years so long as this policy remains in effect, compounding the benefits over time.

I am pleased to make this study available to the Congress and the public to demonstrate the powerful economic benefits produced by restraining federal spending.

Jim Saxton
Vice-Chairman
Joint Economic Committee

The Impact of the Welfare State on the American Economy

One of the most perplexing questions of the late twentieth century is how large the Federal government of the United States should be. At the beginning of the post-World War II era it commanded about one-seventh of the nation's Gross Domestic Product while, in recent years it has surged toward a one-fourth share. The growth in the size of the Federal government in this time is something of a continuation of a trend that began somewhat earlier. For example, in 1929, Federal government expenditures accounted for only slightly more than one-fortieth (2.6 percent) of Gross Domestic Product. These data raise two issues: what has been the impact of growth in the Federal government on the American economy, and why has the government grown so much.

The Economic Impact of the Federal Government

Much of the increase in the size of the Federal government has been justified on the grounds that it would lead to a more efficient economy. However, this is a questionable proposition. Not that government has no role to play in an economic system. There are things it can do to enhance the functioning of an economy, such as providing for the common defense, establishing a legal framework for resolving disputes, constructing a basic infrastructure, and supervising some minimum safety net. These are the positive benefits of government. However, they can be substantially negated if it expands inordinately. Excessive taxation, over-regulation, profligate spending and special favors for privileged interest groups may have a negative effect on the growth of the productive sector.

In the strictest economic sense, the positive effects of government tend to reduce the costs of producing goods and services, thereby raising output and lowering prices. This increases the sum total of what economists call consumer and producer surplus. However, when government has a negative impact on the economy, costs of production are increased, prices rise, and the total volume of consumer and producer surplus declines. This can be viewed as the "deadweight" loss to the economy of government activities.

What is critical in evaluating the impact of the growth in the Federal government on the American economy is the net effect of its positive and negative contributions. When government is small, additions to it are likely to improve the society's economic performance. However, as it becomes larger and larger, the gains it provides become smaller and smaller until they disappear entirely. Beyond that point, further increases in the magnitude of government actually harm the economy.[1] What this implies is a systematic relationship between the size of government and the economic performance of a nation. At low levels of government activity, its net contributions are positive, but at high levels, they become negative. Figure 1 shows a representative version of such a relationship.

The availability of numerical data describing government expenditures and levels of income and output make it possible to statistically evaluate the conceptual framework provided in Figure 1. For

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[1] Such a relationship is described in Dick Armey, **The Freedom Revolution** (Washington, D. C.: Regnery Publishing Company, 1995), pp. 91-93.

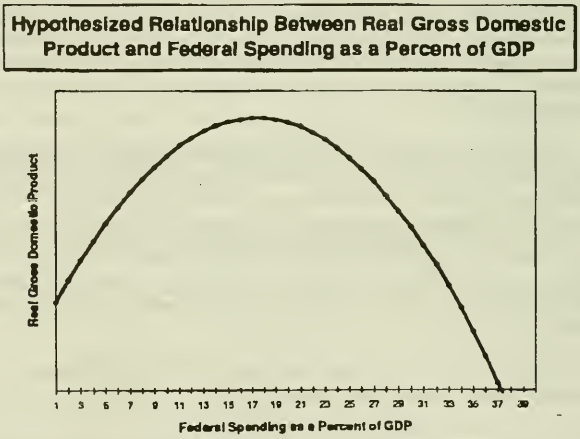
this purpose, a standard measure of overall economic activity, Gross Domestic Product (adjusted for the effect of inflation), will be used to represent the level of output in the American economy. In addition, the national income and product account estimates of government spending will be used to measure the size of the Federal government. The specific estimate will be its spending expressed as a percentage of Gross Domestic product. The time period for which the data have been assembled is 1947 through 1994.[2]

The major problem is one of describing a specific functional relationship between spending as a proportion of Gross Domestic Product and the level of real Gross Domestic Product that is capable of expressing the patterns shown in Figure 1. A simple way of doing this is to postulate a statistical estimating equation that has the size of the Federal government as an independent variable and real output as a dependent variable. In addition, the size of government variable must be introduced in a quadratic fashion, as follows:

$$(1) \qquad O = a + bG - cG^2$$

where O represents real output in the economy and G indicates federal government spending as a percentage of Gross Domestic Product.

Figure 1



[2] We do not use years earlier than 1947 because of serious problems that we feel exist in the data for the World War II years and 1946. For a description of these difficulties, see our "The Great Depression of 1946," **Review of Austrian Economics**, Vol. V, No. 2, (1991).

A few words of explanation about expression (1). Notice that G appears twice on the right hand side, first in a linear fashion and second as the square of itself. Also, the signs of the two terms are opposite. The positive sign on the linear form is designed to show the beneficial effects of government spending on output, while the negative sign given to the squared term means that this variable should measure any negative effects associated with increases in the size of government. Since the squared term increases in value more rapidly than the linear term, the presence of negative effects from government spending will eventually outweigh the positive impact, producing the downward sloping portion of the relationship shown in Figure 1.

In addition, two other factors that might influence the behavior of real output over time need to be taken into account. First is growth over time in real output. It is measured by including a simple measure of the passage of time which takes the value one in 1947, two in 1948, and so on, through 48 in 1994. Second is the possibility of cyclical variations in real output. To control for this, the unemployment rate is included as an independent variable in the estimating equation. Of course, it is expected that time will be positively and unemployment negatively related to changes in real output. Thus, the final form of a statistical estimating equation designed to explain variations in the level of real Gross National Product over the period 1947 through 1994 is:

$$(2) \quad O = a + bG - cG^2 + dT - eU,$$

where T denotes the time variable and U the unemployment measure.

The results of statistically estimating expression (2) are reported in Table 1.[3] All the independent variables are statistically significant at the one percent level or beyond. The results shown in Table 1 provide enough information to permit estimating an empirical version of Figure 1. Such a curve peaks at a Federal government share of resources of 17.57 percent.[4] In one sense this can be thought of as the "optimal" size of the Federal government in the United States.[5] However, this is true only if government spending is not treated as a "cost" of producing output. This distinction is an important one. If government spending is perceived to be a cost of producing output, the optimal level of spending will occur where the additional output associated with an increase in government spending is just equal to the additional cost of that spending.[6]

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[3] Expression (2) was estimated using ordinary least squares regression techniques. Cochrane-Orcutt adjustments were made to resolve any potential problems of autocorrelation. The Cochrane-Orcutt adjustment terms are not reported here.

[4] Emphasizing taxes, rather than spending, Gerald Scully reaches similar conclusions. See his **What is the Optimal Size of Government in the United States?**, NCPA Report No. 188 (Dallas, Texas: National Center for Policy Analysis, 1994). Scully focuses on all government activity, not just federal.

[5] Mathematically, the thresbold point can be derived by differentiating expression (2) with respect to G, setting the result equal to zero, and solving for G. The result is -b/2c.

[6] This is the economist's familiar notion of maximization. In effect, this argument states that the optimal size of the Federal government will be that at which the marginal benefit (in terms of

Table 1

Regression Analysis Used to Explain Variations In Real Gross Domestic Product, United States, 1947-1994

Regression Term	Regression Coefficient	t-Statistic
Constant	-858.06	1.24
Federal Spending as a Percent of GDP	122.29	3.36
Square of Federal Spending as a Percent of GDP	-3.48	-3.62
Time	122.28	9.39
Unemployment	5.64	7.63

* Regression statistics are as follows: R^2=0.9993; Adjusted R^2=0.9992; Durbin-Watson Statistic=1.97; Arima adjustment=(2,0); and F-statistic=9703.76

Using the information reported in Table 1, it is possible to calculate both the additional benefits of government spending and the additional costs associated with it for all levels of such spending. This requires assuming the values for the other variables in expression (2) that existed in 1994. When these calculations are made and the additional benefit and additional cost schedules are graphed, the result is as shown in Figure 2. Under this set of assumptions, the optimal level of Federal government spending as a share of Gross National Product occurs where the two curves cross, which is somewhere between 10 and 11 percent, or less than half its present size.

Since treating all Federal government spending as a cost of producing output may ignore certain positive services that are not directly related to making the process of production more efficient, it was decided to work with the first of these concepts of optimality. Clearly, the information reported in Table 1 confirms the idea that the American Federal government has become too large - by a factor of about one-third - thereby creating significant economic inefficiencies. What this indicates is simple. As the Federal government grows, it rapidly exhausts the opportunities for contributing to the stability that is necessary for rapid economic growth. Consequently, it must venture more and more into the realm of activities that have the net effect of discouraging economic activity, things such as economic regulation and the use of the government's taxing and spending power to redistribute income. Some standard statistics, which are summarized in Table 2, will demonstrate just how this transformation has taken place in the United States. Go back to the immediate post-World War II era, after the military stand-down following the war had been completed, say to fiscal year 1948. Federal government spending totaled $29.8 billion, 12.1 percent of Gross Domestic Product. Less than a third of it ($9.1

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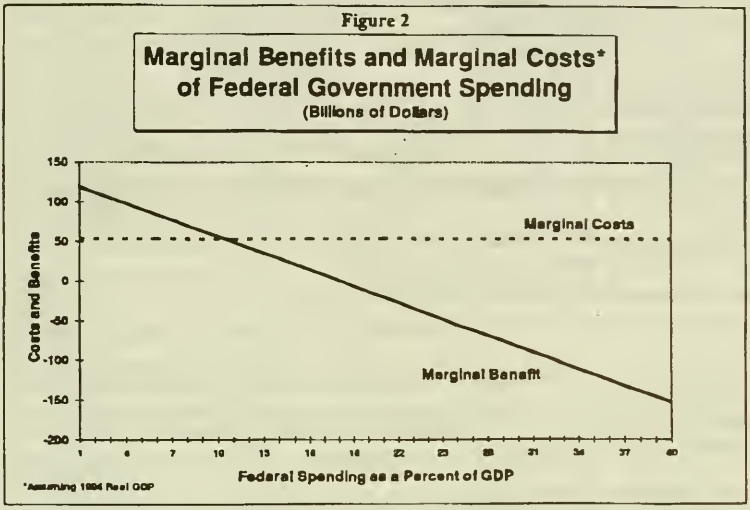
additional real output) is just equal to the marginal cost incurred. A technical point: For this reasoning to be valid, certain other conditions must be satisfied. As will be seen shortly, they are.

billion) was for national defense. Three broad categories of social spending - health, income security, and social security - absorbed slightly more than ten percent of outlays, totaling about $3.3 billion or about 1.3 percent of Gross Domestic Product. We focus on these as being representative of the modern welfare state. To be sure, they do not include all social spending, but they are indicative of the broad trends in the character of federal spending. The growth in the social spending category at this time was modest. In the fiscal years from 1940 to 1948, only 8.4 cents of every additional dollar of federal spending had gone for this purpose.

Figure 2



That last statistic, and its behavior subsequent to 1948, is perhaps the key to understanding the changing nature of the role of government in American life. In the twelve years from 1948 through 1960, it more than triples. Over a fourth (26.4 cents) of every new dollar of federal spending went to this variant of social spending. This is just the beginning. Between fiscal years 1960 and 1970, over a third of new spending is in this category and in the interval 1970 through 1980, it is more than one-half.[7]

There is a brief respite in the 1980s. From 1980 to 1990, only 44.0 cents of each new dollar of federal spending is for health, income security, and social security. However, this is just a temporary departure from the long term trend. In the five years from fiscal 1990 through fiscal 1995, outlays on these categories of spending rise by $1.067 for every additional dollar of all federal spending. The combined effect for the period since 1980 is 61.7 cents of new social spending per dollar of further federal spending.

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[7] Beginning with 1966, health spending includes outlays under the Medicare program.

Table 2

Federal and Social* Spending Statistics, United States
Various Fiscal Years, 1940-1995

Fiscal Year	Federal Spending ($Billions)	Federal Spending As Percent of GDP	Social Spending ($ Billions)	Social Spending As Percent of GDP	Increase in Social Spending per Dollar Increase in Federal Spending
1940	9.5	9.9	1.6	1.7	na
1948	29.8	12.1	3.3	1.3	0.094
1960	92.2	18.3	19.8	3.9	0.264
1970	183.6	18.9	58	6.2	0.344
1980	590.9	22.3	260.4	9.8	0.513
1990	1252.7	22.9	551.4	10.1	0.44
1995	1514.4	21.8	830.4	11.3	1.067

* Defined as the sum of health, income security, and social security expenditures. Beginning with 1966, health spending includes outlays on the Medicare program.

Source: United States Treasury and Office of Management and Budget

The overall impact of these changes is dramatic. As of fiscal 1995, 11.3 percent of Gross Domestic Product goes to these three categories, compared to 1.3 percent in 1948. Put another way, in fiscal 1948, about one dollar in nine of federal spending was for these social purposes. By fiscal 1995, five dollars out of every nine were devoted to these pursuits.

The critical dimension of this shift in the nature of federal spending is the preponderance of transfer payments in this rapidly growing sector. The negative economic disincentive effects associated with income transfers have been well documented.[8] An increasing emphasis on income transfers exerts a "drag" on the economy and goes far in explaining the statistical results reported earlier. The rapid growth in the American welfare state has been depressing the level of national output for some time.

[8] For example, see Sheldon Danziger, Robert Haveman, and Robert Plotnick, "How Income Transfer Programs Affect Work, Savings, and Income Distribution: A Critical Review," **Journal of Economic Literature**, September 1981. They conclude that the cumulative effect of income transfers in the United States, at that time, had been to reduce the total supply of labor by 4.8 percent. Similar effects were observed in Lowell Gallaway, Richard Vedder, and Robert Lawson, "Why People Work: an Examination of Interstate Variations in Labor Force Participation," **Journal of Labor Research**, Winter 1991, pp. 47-59.

Table 3

Annual Dollar and Percentage Losses of Gross Domestic Product Due to Government Being Too Large, United States, 1965-1994

Year	Loss of GDP ($ Billions)	Percentage Loss of GDP
1965	0.09	0
1966	5.44	0.21
1967	25.64	0.95
1968	23.69	0.85
1969	18.94	0.66
1970	32.5	1.13
1971	28.66	0.97
1972	33.04	1.06
1973	20.97	0.64
1974	39.72	1.22
1975	101.16	3.14
1976	74.7	2.21
1977	56.42	1.6
1978	41.33	1.12
1979	38.68	1.02
1980	89.34	2.37
1981	103.43	2.69
1982	165.81	4.41
1983	175.23	4.49
1984	127.82	3.08
1985	144.4	3.37
1986	147.66	3.35
1987	121.07	2.67
1988	89.01	1.89
1989	84.58	1.76
1990	104.88	2.14
1991	121.13	2.49
1992	114.12	2.29
1993	84.46	1.65
1994	68.19	1.27

Annual Estimates of Lost Output Associated with an Oversized Government

Specific estimates of the annual losses in real Gross Domestic Product that accompany a Federal government that is either smaller than or larger than the 17.57 percent share that marks the transition between government being a positive force and its pulling the economy down can be developed from the empirical findings reported earlier. 1965 is the year in which government spending was approximately "optimal." Since then, it has exceeded the 17.57 percent threshold level in every year. The year by year annual losses of output, beginning with 1965, are shown in Table 3, both in constant dollar terms and as a percentage of real Gross Domestic Product. The cumulative losses in real output as the result of the Federal government spending share of Gross Domestic Product being too large amount to about 2.3 trillion dollars in the 1965-1995 period. The behavior of the percentage loss in real output statistic over time is shown in Figure 3.

The pattern shown in Figure 3 is quite consistent with the historical discussion of the rise of large government in the United States. During the bulk of the early post-World War II era, the size of the federal government is reasonably close to optimal, as that term is being used here. But, beginning with the mid-1960s it starts to depart substantially from that level and by the mid-1970s is dragging the economy down by two to two-and-one half percent. There is a brief improvement, but then the losses begin to mount in 1980, 1981, and 1982, exceeding four percent in the last of these years. The next seven years, though, see a significant decline in the negative impact of the size of government on the economy. It is in this interval that the federal government share of Gross Domestic Product declines by nearly two full percentage points.

Figure 3

Big Government in Perspective

The picture of how large government negatively influences the level of economic activity in the American economy is now clear. When government grows beyond the level that is optimal for the economy, it introduces inefficiencies that increase the cost of producing goods and services. To put in perspective the magnitude of these inefficiencies, ask the question, "What would be the effect of a $100 billion dollar reduction in Federal government spending?" At 1994 levels of national output, that would amount to about a 1.5 percentage point reduction in spending as a percent of Gross Domestic Product. Since Federal government spending stood at 22.0 percent of Gross Domestic Product in 1994, a $100 billion reduction in spending would lower its percentage equivalent to 20.5. Substituting 20.5 percent for 22.0 percent would have the direct effect of increasing Gross Domestic Product by $38 billion. Put another way, a $100 billion decrease in Federal spending would result in a canceling of

$38 billion of deadweight losses in the economy that are attributable to government being larger than desirable. Thus, the bottom line is that for every dollar reduction in current levels of Federal government spending, other things remaining the same, Gross Domestic Product will increase by 38 cents during the year of the reduction.[9] On a per capita basis, this amounts to about a $145 dollar gain in real output.

Table 4

Current Dollar Gain and Discounted Present Value of Current Dollar Gain Associated With a Permanent One Dollar Reduction In Federal Government Spending in the United States

Year in Budget Plan	Current Dollar Gain	Discounted Present Value of Current Dollar Gain
1	0.38	0.38
2	0.37	0.35
3	0.36	0.32
4	0.35	0.29
5	0.34	0.27
6	0.33	0.25
7	0.32	0.23
Seven Year Total	2.45	2.09

If the reduction in spending is a permanent one, the longer term gains in succeeding years will be even greater. Given the emphasis in current budget debates on balancing the budget within seven years, we have estimated the impact of a permanent reduction in spending over such a period. The year-by-year results are reported in Table 4. Two estimates are provided, a current dollar one and another that measures the present value of the output gains discounted back to the initial year of the spending reduction. For the first of these, five percent annual growth in Gross Domestic Product (2.5 percent growth in prices plus 2.5 percent real growth) is assumed. For the second, the basic assumption is that a six percent discount rate is appropriate.

The current dollar effects of a permanent reduction in spending "decay" over time because, as Gross Domestic Product rises, a given reduction in spending represents a smaller percentage of national output. Nevertheless, over a seven year period, the cumulative current dollar effect on output of permanently reducing federal spending is $2.45 for every dollar spending is decreased. The discounted present value of these gains is $2.09 per dollar of spending reduction. Thus, assuming a population of approximately 260 million, the discounted present value of a $100 billion decrease in

[9] Interestingly, Ballard, Charles L., John B. Shoven, and John Whalley, "General Equilibrium Computations of the Marginal-Welfare Costs of Taxes in the United States," **American Economic Review**, March 1985, find that the marginal excess burden (deadweight loss) associated with taxation could fall in the range of 20 to 50 cents per dollar of taxation. Their methodology is that of a computable general equilibrium model. Such models are capable of incorporating various dynamic effects of increases in government taxation and spending. The correspondence between their estimates of deadweight loss and ours is reassuring.

federal spending would be the equivalent of an $800 lump sum payment to every person in the United States **in addition to the direct gains that would accrue to the private sector as the result of the reduction in government spending freeing up private sector income.** Clearly, the potential long-term output gains from reductions in federal spending are substantial.

Some Additional Considerations

The estimates of the inefficiencies introduced by the pure size of the federal government that have been presented are absolute minimum values. For one thing, much of the actual government spending produces output whose true value is less than the cost of producing it. Yet, a portion of this spending is counted on a cost of production basis as adding to Gross Domestic Product.[10] Even more of a problem is the presence of government activity that impacts on the production of goods and services but is not reflected in the government spending statistics. For example, any regulation that requires private citizens to incur certain costs or outlays is the exact equivalent of government taxing that income away from citizens and spending it for them. In recent years this new form of "silent" taxation has become more popular with elected officials. As an example, consider the cost to the private sector of simply doing the paperwork required to satisfy various government regulations. In addition, there are such mandates as minimum wage rates, expenses necessary to meet environmental regulations, and the costs to business of meeting certain requirements concerning access for the handicapped. All of these represent some form of government control over the economy's resources and should be included in any measure of the proportion of the country's resources that are in the hands of the government.

More of these programs that constitute silent government taxation and spending have been suggested. The beauty of them for the legislator is their silent quality. Using this technique, it is possible to levy taxes in a far less obtrusive fashion than actually voting up or down for additional levies on the public. The favorite target for these exactions is the business sector of the economy. Business is widely perceived to have "deep pockets" and thus able to bear the cost of these various programs, all of which are justified by the usual rhetoric claiming that they are vital and essential to the well-being of the nation. However, there is no such thing as a "free lunch." The costs of these silent taxes are ultimately borne by resource owners, including individual workers.[11]

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[10] The portion of government spending that is categorized as government purchases of goods and services is included in the calculation of the statistic Gross National Product.

[11] An example of this phenomenon is illustrated in Richard Vedder and Lowell Gallaway, **Laws, Litigation and Labor Markets: Some New Evidence** in **The Economic Effects of Employment Law in California: The Unintended Consequences of Good Intentions**, introduction by Steven Hayward (San Francisco: Pacific Research Institute, 1995). This study analyzes the negative wage and employment effects of the change from a legal doctrine of "employment at will" to one that permits employees to claim "wrongful termination."

A Brief History of the Growth in the Size of the Federal Government

How did we get to the present level of government spending? Why has the country moved away from David Thoreau's principle, "That government is best which governs least." First were structural changes in the nature of the American governmental system, particularly those associated with the year 1913, when the income tax amendment to the Constitution was ratified and the Federal Reserve system went into operation. The first of these ultimately would provide a large part of the wherewithal to finance the expansion of government and the second would be both an instrument of control and a mechanism to facilitate the creation of government debt, also used to pay the bills for an ever growing national government.

Second, the experiences associated with managing the American economy during the first of the two World Wars served to whet the appetite of those with an urge to get their hands on the levers of power in American society. The planning atmosphere of the years 1917-1918 was infectious and would have a lasting effect on many people of influence in the years to come.[12]

Third, there were the events of the Great Depression of the 1930s, a crisis created in no small way by the activities of the Federal Reserve and the economic policies of a control minded President, Herbert Hoover.[13] The traumatic events of that era provided an opportunity and a rationale for a substantial expansion of the role of the Federal government. By 1939, the share of Gross Domestic Product absorbed by Federal expenditures had risen to 9.9 percent.

The final links in the chain of circumstances that would justify greater intrusions of government into the American economy came from the intellectual community. On the technical side was John Maynard Keynes's **The General Theory of Employment, Interest and Money**, published in 1936, which argued that public spending was a perfect substitute for private spending in terms of its effect on the overall economy.[14] From a broader perspective, Keynes's economic prescriptions were given greater pertinence by the "stagnationist" notions that dominated much of the American intellectual community at the close of the decade of the 1930s. Perhaps the leading proponent of the "stagnationist" idea was Alvin Hansen. In his Presidential address to the American Economic Association in 1938, he maintained that a combination of the closing of the American frontier and a

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[12] For a discussion of the impact of World War I on the attitudes of influential business and political leaders, especially during the Great Depression years, see William E. Leuchtenberg, "The New Deal and the Analogue of War," in John Braeman, Robert E. Bremner, and Everett Walters, eds., **Change and Continuity in Twentieth Century America** (Columbus, Ohio: Ohio State University Press, 1964), pp. 81-143.

[13] For a detailed description of the sequence of events which triggered the Great Depression, see Richard Vedder and Lowell Gallaway, **Out of Work: Unemployment and Government in Twentieth Century America** (New York: Holmes and Meier, 1992), Chapter 5.

[14] Keynes, John Maynard, **The General Theory of Employment, Interest and Money** (New York: Harcourt Brace, 1936).

slowing in the rate of population growth meant an absence of the private investment opportunities that had been the driving force in earlier economic expansion in the United States.[15]

The "stagnationist" argument integrated quite closely with the Keynesian framework. If private investment was doomed to be inadequate to provide further sustained economic growth, a la Hansen, the simple solution would be to supplement it with Keynes's perfect substitute, public spending. The vindication of this argument seemed to arrive with the onset of World War II. Even before American entry into that conflict, there had been a large increase in public spending at the national level. In calendar year 1941, Federal government expenditures amounted to 16.4 percent of Gross Domestic Product. It did not go unnoticed that the economy seemed to thrive. The unemployment rate in 1941 is estimated to have been 9.9 percent, the lowest since 1930. What followed seemed to be a testimonial to the efficacy of the Keynes-Hansen analysis. With all-out mobilization, government spending surged and the unemployment rate plummeted, falling to as low as 1.2 percent in 1944.

The impact of World War II on the American economy was widely interpreted as a vindication of Keynesian economic principles. This suggested that it was possible to manage the overall economy through a judicious use of public spending. It also strongly implied that problems might lie ahead as the war reached its climax. In particular, what would happen to the American economy when the massive military expenditures of the war years were no longer necessary. As early as 1943, Hansen was expressing Keynesian-like concerns, remarking, "When the war is over, Government cannot just disband the Army, close down munitions factories, stop building ships, and remove all economic controls."[16]

Peace did come and with it all the worries implied by the Hansen statement. By now, a substantial technical apparatus had been constructed to supplement Keynes's initial work and the economics profession had been overwhelmed by a tidal wave of Keynesian sentiment, especially among its younger members.[17] Within that framework, disaster loomed, unless the government took strong action. More than just professional economists shared this concern. President Harry Truman, speaking to Congress a few days after the Japanese surrender closed the door on World War II, when talking about the post-war reconversion said, "Obviously, during the process there will be a great deal of inevitable unemployment."[18] In the media, **Business Week**, on September 1, predicted that Gross National product in 1946 would be twenty percent less than it was in 1944 and that unemployment

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[15] Alvin H. Hansen, "Economic Progress and Declining Population Growth," **American Economic Review**, vol. 29, March 1939.

[16] This comment is included in a publication for the National Resources Planning Board, as quoted by Hugh S. Norton, **The Employment Act and the Council of Economic Advisers, 1946-1976** (Columbia, S. C.: University of South Carolina Press, 1977).

[17] For an intriguing reflection on the changes in the thinking of economists wrought by Keynes, see Paul A. Samuelson, "The General Theory," in Seymour Harris, ed., **The New Economics** (New York: A. A. Knopf, 1947).

[18] **New York Times**, September 7, 1945, p. 16, col. 3.

would peak at nearly nine million or roughly at 14 percent of the expected civilian labor force.[19]

With rare exceptions, doom and gloom were in the air.[20] The need for some form of government intervention seemed obvious to many. But what? How should the Federal government intervene? In the spirit of the times, Keynesianism, whatever government did should impact on what was now known as aggregate demand, that curious combination of private and public spending that, in a reversal of Say's Law, would supposedly create its own supply. Yet, there seemed to be some uncertainty in political circles about what to do. At times, President Truman apparently was enamored of aggregate demand notions, calling for an increase in the minimum wage on the grounds that, "...the existence of substandard wage levels sharply curtails the national purchasing power and narrows the markets for the products of our firms and factories."[21] At other times, though, his primary concerns were the non-Keynesian notion of balancing the budget or, better yet, running a budget surplus to reduce the national debt.[22] Elsewhere, arguments were being made for some form of government intervention in the economy. In late August, Paul G. Hoffman, Chairman of the Studebaker Corporation and head of the Committee for Economic Development, recommended federal aid to assist the newly created jobless to move to areas where jobs existed.[23] And, within the Federal government there was a call by the ranking Republican member of the House Ways and Means Committee, Harold Knutson, for a 20 percent reduction in income taxes and Truman's request for the passage of a Full Employment Act that would mandate counter-cyclical fiscal policy - public spending - in case of an emergency.[24] Nothing came of the first of these, but the latter led to the passage of the Employment Act of 1946, which established the Council of Economic Advisers and the Joint Economic Committee of Congress.

In many ways, the Federal government seemed to be drifting into the post-World War II era. This was largely the result of economic indecision on the part of Harry Truman. What this ultimately translated into in terms of a national economic policy was a determination to maintain the **status quo**,

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[19] **Business Week**, September 1, p. 9.

[20] For detailed discussions of the nature of the economic forecasts of this period, see Martin Bronfenbrenner, "The Consumption Function Controversy," **Southern Economic Journal**, January 1948, pp. 304-20, and Michael Sapir, "Review of Economic Forecasts for the Transition Period," in Vol. XI, **Studies in Income and Wealth** (New York: National Bureau of Economic Research, 1949).

[21] **New York Times**, September 1, p. 16, col. 3.

[22] See Alonzo Hamby, **Man of the People** (New York: Oxford University Press, 1995), p. 385.

[23] **New York Times**, August 28, 1945, p. 38, col. 4.

[24] **New York Times**, August 28, 1945, p. 1, col. 2. Knutson repeated his call for a 20 percent reduction in the individual income tax plus an end to the corporate excess profits tax in late September. Both suggestions were ignored. Truman's request for a Full Employment Act is reported in **New York Times**, September 7, 1945, p. 16, col. 1.

that is to keep the wartime economic controls in place as long as possible. No tax cuts, though, despite a rapid decline in Federal government spending. In the single year 1946 expenditures fell by more than fifty percent over the previous year. Not unexpectedly, the prevalence of Keynesian ideas led a number of major economists to forecast a severe post-war economic decline. However, surprisingly, to the Keynesians, that is, the economy made the transformation to peacetime conditions in a surprisingly smooth fashion. Disaster did not occur as the Federal government did exactly what Alvin Hansen had said it could not do: It disbanded the army, closed the munitions factories, and stopped building ships. All that was left of Hansen's economic recommendations were the wartime controls. And they went by the board in mid-1946 simply because Truman would not accept any watering down of them and the Congress was unable to override his veto of legislation that would have done just that. Suddenly, on July 1, 1946, all of Hansen's worst fears had been realized.

In the aftermath of the absence of substantial government intervention in the economy, there was a marked increase in price levels and a rise in unemployment. However, the unemployment rate increased only to 3.9 percent for 1946, stayed at the level in 1947, and averaged 3.8 percent in 1948. The feared immediate post-World War II depression had not materialized, despite federal government expenditures in 1948 being less than one-third as large as they were in 1944 and despite the disappearance of the wartime controls. None of the Keynesian predictions had been validated. Yet, by now the commitment to Keynesianism was so strong that an **ad hoc** explanation for the relatively easy transition from war to peace that could be used to reconcile actual events with Keynesian theory was developed. It emphasized the role of "pent-up" consumer demand resulting from the lack of availability of goods and services during World War II. To be sure, people wanted more consumer goods (don't they always?) but the empirical evidence simply does not support the idea that there was some dramatic shift in consumption that explained the absence of a serious economic downturn following the war.[25]

With the passage of the Employment Act of 1946, in February of that year, the last element in the system designed to manage the American economy was set in place. After a prolonged debate about the definition of terms such as "full employment" and what the character of the institutional arrangements for implementing it should be, the legislation was agreed upon. It committed the Federal government to assuming responsibility for the provision of employment opportunities to those "able, willing, and seeking to work." In addition to establishing the Council of Economic Advisers and the Joint Economic Committee of Congress, it mandated the submission of the **Economic Report of the President** to Congress. From this moment on, Federal involvement in the direction of the American economy was a legislative requirement, although the degree of intervention was a matter of choice on the part of a President and his Administration.

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[25] In an amazingly rapid turnaround, the process of reconversion was largely complete in early 1946. Nearly seven million people had left the armed forces, and government spending had fallen well over 90 percent of the way from the wartime peak to what would be the postwar low in 1947. In addition, monetary growth also contracted sharply. For example, bank reserves had declined by about sixty percent. As to unemployment, it was slightly in excess of four percent. Yet, at this time, consumer spending was still well below normal peacetime levels. For a detailed discussion of the "pent-up" demand thesis, see Vedder and Gallaway, **Out of Work**, **op. cit.**, Chapter 8.

The stage was now set for the emergence of what Herbert Stein calls a "consensus" with respect to the use of fiscal policy.[26] Remarkably, that consensus ignored the primary lesson of the immediate post-World War II transition to peace, the lack of a need for an infusion of government spending in order to sustain the American economy. Instead, what emerged contained the seeds of a future explosion in the size of the Federal government. At its heart was the abandonment of the notion of balancing the Federal budget, either in the immediate term or over some longer period of time. Now, the emphasis would be on balancing the budget only in times of prosperity, if then. In the 25 years subsequent to 1949, there are twenty years of budget deficits, for the most part small, with outlays usually being within ten percent of receipts. However, there were exceptions, such as 1959, 1968, 1971, and 1972. In these four years expenditures were more than ten percent greater that receipts. The justification for this new consensus was that it provided a greater government capability to manage the economy and produce conditions of prosperity. Amazingly, the evidence that the manipulation of government expenditures was important to maintaining prosperity was almost non-existent at the time the consensus emerged. As already described, in the years immediately prior to 1949, there is the most dramatic fiscal shift in history. Federal government expenditures go from being **more than twice receipts to being about seventy percent of receipts.** The total fiscal shift in this period represented about one-fourth of the typical year's Gross Domestic Product. In today's terms, this would mean a fiscal shift of approximately one-and-a-half **trillion** dollars. The result of this Draconian slashing of federal expenditures? The previously indicated unemployment rates that did not, on average, exceed four percent during the three years that followed the onset of this change.

Still, the fascination with government spending as a source of prosperity was there. In many ways, the wish seemed to be father of the thought. Later, the recoveries from the relatively mild business cycle downturns of 1949, 1954, and 1958 would be regarded as something of a Keynesian **tour de force**, even though the evidence indicates that "discretionary" fiscal policy changes typically amounted to about one-tenth of one percent of Gross Domestic Product.[27] The reality was that these business cycle recoveries were a testimonial to the natural recuperative powers of the private economy.[28]

There was still one more genie to be let out of the bottle. Through the 1950s the phenomenon of inflation still was widely regarded with distrust. However, toward the end of that decade the intellectual community weighed in with an argument that inflation might not be all that bad. Perhaps the quintessential statement of the Keynesian, or by now neo-Keynesian, theory is the relationship

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[26] Herbert Stein, **The Fiscal Revolution in America** (Chicago, Ill.: University of Chicago Press, 1969), Chapter 9.

[27] See Wilfred Lewis, Jr., **Federal Fiscal Policy in the Postwar Recessions** (Washington, D. C.: The Brookings Institution, 1962).

[28] For a more detailed discussion of this point, see Vedder and Gallaway, **Out of Work**, **op. cit**, Chapter 9.

known as the Phillips curve.[29] The implication of the Phillips curve in its original form was that some extra output and employment could be bought by simply accepting some degree of price inflation. This was simply too attractive a possibility to ignore. From the mid-1960s on, the rate of price inflation escalated inexorably until the early 1980s. Over the twelve years 1953-1964 prices rose by 1.3 percent a year. From 1965 to 1969, the annual increase was 3.4 percent; from 1970 to 1974, 6.1 percent; and 1975 to 1979, 8.1 percent.

Accompanying the increase in the rate of inflation was a steady growth in the size of the Federal government. This was no accident. Given the progressive nature of the American income tax system and the lack of indexing for changes in the price level during this period, inflation was systematically operating to increase Federal government revenues as a share of Gross Domestic Product. This is the familiar notion of "bracket creep." Of course, this translated into additional government spending. Whereas the Federal share of Gross Domestic Product was 18.7 percent in the interval 1953-1964, it rose to 19.3 percent from 1965 to 1969; 19.7 percent from 1970 to 1974; and 21.5 percent over the years 1975 to 1979.

Towards the end of the period of rising rates of price inflation, budget deficits also began to rise. Excesses of expenditures over receipts of more than 10 percent had occurred four times in the 25 year period 1950-1974. After 1974, there is only one year when this is **not** true. At this point, the revenue restraints that limited the growth in the size of the Federal government in earlier years were non-operative. Predictably, the average share of Gross Domestic Product absorbed by Federal government expenditures in the 16 years following 1979 increased to 22.9 percent.

What to do About the Size of Government

What can we say in closing? Clearly, the historic growth in the relative size of the Federal government has long since reached a critical stage. It has become oversized, at times by more than a third, and currently by more than a fourth. In the process, it has become the source of substantial deadweight losses for the American economy. The message from all this is quite obvious. The time has come to rein in the spending activities of the Federal government. If this is done, the overall economy will benefit and there will be an infusion of income into the private sector of the economy. Our findings indicate that for every dollar government spending is reduced and a dollars worth of resources is freed up to be used by the private sector, an additional 38 cents of output and income will be created in the initial year of the reduction and, over a seven year period, the total increase in income will be $2.45. This constitutes a powerful argument for reducing levels of Federal government spending.

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[29] The most influential argument in this respect is contained in Paul Samuelson and Robert Solow, "The Analytics of Anti-Inflationary Policy," **American Economic Review**, May 1960, pp. 177-194.

PREPARED STATEMENT OF HON. ROD GRAMS, A U.S. SENATOR FROM THE STATE OF MINNESOTA

Mr. Chairman, distinguished members of the Senate Judiciary Committee, I thank you for allowing me to appear before your Committee today to discuss the "Taxpayer Protection" Balanced Budget Amendment (S.J. Res 22). Having introduced this legislation last January in advance of floor debate on the Balanced Budget Amendment, I am pleased to have this opportunity to testify on the merits of this bill.

As the members of the Committee may recall, this legislation calls for a balanced budget amendment to the Constitution. And I am pleased to have the support and cosponsorship of the distinguished Assistant Majority Leader, Senator Lott, and my colleagues, Senators Smith, Mack, Frist, Inhofe and Thomas.

Senate Joint Resolution 22 is the legislation the American people are calling for. It balances the budget * * * but ensures that it is not balanced on the backs of the American taxpayers.

I believe this hearing is quite timely, because by tonight at midnight, taxpayers across this nation will be filing their federal income tax returns and realizing exactly how much they are being asked to pay for their government. And it will be this realization, that will solidify their support behind the "taxpayer protection" balanced budget amendment.

There is no question that Congress must pass a balanced budget amendment and send it to the states for ratification. For years, Washington has been racking up deficits. In the process, we've racked up a four and a half trillion national debt. And sadly, we've got very little to show for it.

Without the balanced budget amendment, Congress will continue its deficit-digging, debt-building ways. That's bad news for the taxpayers and worse news for our children.

Yes, we need the balanced budget amendment * * * but not if Congress is allowed to use it as an excuse to raise taxes to mask its continued penchant for spending.

If you look at every so-called "deficit reduction" package Congress has passed in the last decade, you'll find that each one follows a consistent formula. Raise taxes now. Cut spending later. That was of course, until Congress passed the Balanced Budget Act of 1995. Tragically, that plan was vetoed by the President.

Once again, Congress is gearing up to consider a budget resolution. And there is talk of another vote on a balanced budget constitutional amendment. Therefore, this body has the opportunity to put an end to the madness that continues to drain the American Taxpayers.

That's why I introduced the "taxpayer protection" balanced budget amendment in the Senate last year. My amendment would require a three-fifths supermajority vote in both houses of Congress to raise taxes.

A supermajority requirement is the best way to show the American taxpayers that Congress is serious about balancing the budget through spending cuts * * * and not through higher taxes.

That's what I promised the taxpayers of Minnesota during my campaign for the U.S. Senate. That's what they elected me to do. That's what my bill delivers.

Is there enough support in Congress to pass it? If we listen to the folks back home, there sure ought to be.

And today, the House of Representatives will be taking the first step towards that goal—by voting on virtually identical legislation authored by Representative Joe Barton (R–TX).

A balanced budget has got to be achieved through cuts in government spending, taxpayers have told the ACU—even it means cuts in essential government programs.

Americans are willing to do that * * * but they aren't willing to be patsies for a big-spending government that just hasn't learned when to say "no."

The supermajority requirement is simply good government, and Americans support it just as they support the $500 per-child tax credit. They're tired of watching their paychecks grow smaller while Washington grows bigger.

They voted for change in 1994, and it's our job to see that they get it.

That's what's best for the taxpayers * * * that's what's best for our children * * * that's what's best for Minnesota * * * that's what's best for America.

As members of the U.S. Senate, we should all be closely watching today's vote in the House. We must be prepared to tell our constituents how we will vote on such a measure later this year. And as the sponsor of S.J. Res. 22, I fully support the

House action and will continue to advocate adoption of this amendment by the Senate—I hope my colleagues on this Committee will pledge to do the same.

Again, I thank the Chairman and the Committee for holding this hearing on issues critical to the economic welfare of the American taxpayers. It is truly an historic day for the Congress and even more so for the taxpayers.

Thank you.

Senator BROWN. Our next witness has a very distinguished record of public service, including being counselor to the President, always thought to be a source of wise advice and a frequent witness before this committee.

Lloyd Cutler, why don't you go ahead?

STATEMENT OF LLOYD N. CUTLER

Mr. CUTLER. Thank you very much, Mr. Chairman. Let me say at the beginning that I have no substantial quarrels with the tax policies that are being outlined by Secretary Kemp and Senator Kyl. My quarrel is with the sheer unworkability of this kind of an amendment and the fact that it would put us into a straightjacket that would prevent us from raising or modifying a tax at a time when the majority of the legislators and the public clearly believe such a tax is needed; for example, a new threat from the Soviets or whatever else it might be, short of armed conflict, that makes it necessary to incur additional expenses and necessary because of the budget deficit not to simply borrow the money to incur those expenditures.

I also am a co-founder and secretary of the Concord Coalition, which shares many of the tax policy objectives that Secretary Kemp and Senator Kyl have outlined. As you may know, co-chairmen Warren Rudman and Paul Tsongas have written to each member of the House of Representatives urging a vote against the parallel amendment which is scheduled for a floor vote in the House today.

The gist of the amendment is to reform the existing constitutional procedure for voting on a tax bill or any other bill on the floor of the Senate or the House. It is characterized as a reform, but it reminds me of the 19th century reform bills that were presented to the British Parliament for the purpose of making the election of members more representative and democratic, and a conservative critic was supposed to have said, "Reform, why do we want reform? Things are bad enough as they are."

What is bad enough under the present system, in my opinion, is the growing tendency toward gridlock, especially when the White House is held by one party and a majority of one or both Houses of Congress is held by the other party. This proposed reform embodies a measure that would make the gridlock considerably worse. It would require that any bill to levy a new tax, not just an income tax, a new tax, or to increase the rate or base of any tax may pass only by a two-thirds number of the whole number of each House of Congress, the whole number being 100 in the case of the Senate and 435 in the case of the House.

Now, of course, the present constitutional requirements, after long debate in the Convention, require only that the presence of a majority of the whole number is sufficient for a quorum and that a majority of those present, a simple majority of those present, is enough to pass a bill.

The proposed amendment would change all of that by providing that for tax bills, even though the simple majority needed for the quorum is present, a vote of two-thirds of the whole number is needed to pass the bill. This would mean, Senator Kyl, that if 34 of you simply absented yourselves from the floor and never even cast a vote, a tax bill could not pass even though 66 members voted 66 to nothing in favor of that bill. If you talk about gridlock, that is certainly the way to ensure it, and the absent members don't even need to recall themselves.

Let me give you two examples of how this present tendency to gridlock would be made even worse. First, as you know, the law that created the airline ticket tax expired by its own terms on December 31, 1995, and because of the present budget gridlock and the shutting down of the Government, Congress did not renew the tax before it expired and it has not been collected since the beginning of January 1996. We have probably lost $1 billion a year not collecting that tax, or more.

Allowing this tax to expire was not a deliberate policy judgment of the Congress of the United States. It was a mere happenstance of governmental gridlock. Today, a simple majority of the Senate and House could restore the ticket tax if it felt that the lost revenue was needed, if we are going to be serious about our efforts to reduce the budget deficit. But under the proposed amendment, it would take 67 of the 100 Senators and 290 of the 435 Congressmen to restore this tax which, since it has already expired, would clearly be a "new tax" under the wording of this amendment.

Second, virtually any tax bill, even if it lowers some rates, increases other rates or adds some new tax in order to keep the entire measure either revenue-neutral or to minimize the net loss of revenue that is involved. For example, the present House, as you know, has adopted by mere procedural rule a 60-percent requirement—I think it is 60 percent of those present—in order to pass a bill raising any income tax rate. But the House has had to waive that requirement on at least three major occasions to date. Congressman Skaggs has led a constitutional attack on the validity of that measure, which is clearly constitutionally suspect even though it may be an issue which the courts would decline to adjudicate.

A waiver would also be needed, I think, for almost any version of the flat tax which Secretary Kemp and others have been advocating. I think the lowest rate today is 15 percent. Secretary Kemp, although he hasn't given precise numbers, has said he thought the ideal flat tax would be in the range of 19 percent, or something like that, and a two-thirds vote would be required under this bill, two-thirds of the whole number of members.

Moreover, the exceptions that are provided in section 2 are wholly inadequate. They are limited to cases of actual armed conflict. They do not cover other national security crises such as the one I mentioned earlier. Let us suppose, because of something the Chinese do or some development in Russia, we really do need another extensive and costly rearmament program, although armed conflict has not yet broken out. Are we going to finance that entirely by new debt? Is that a serious way to go about balancing the budget?

The same thing would be true of responding to a recession or a budget impasse. Moreover, with respect to really addressing the budget problems, this amendment would limit the solution of any budget problem to cuts in expenditures. Increases in taxes, even minor adjustments in taxes, would be entirely off the table.

The present Constitution requires supermajority votes in a very limited number of cases, such as the Chair has already observed, and Senator Kyl, where the Framers thought that a high degree of consensus was more important than the gridlock resulting from a failure to obtain the required supermajority, and these supermajority requirements under the present Constitution are limited to such matters as the override of Presidential veto, as has been mentioned; the adoption of new constitutional amendments; the expulsion of a Member; or a conviction by the Senate in the case of an impeachment trial.

If the necessary supermajority is not achieved, the worst that can happen is we are stuck with the status quo, something that the country in those cases can usually survive. But if a constitutional supermajority is required even to pass a tax bill, the Nation itself can be paralyzed, as in the situations I described to you, because once you establish a supermajority, especially this rigorous supermajority of two-thirds of the whole number of both Houses, it is entirely conceivable that while a simple majority of those present and voting could be found to compromise the issue and achieve a result one way or the other, a supermajority cannot be found for that compromise or any other compromise, and the result is sheer impasse. The country is in a straightjacket and can do nothing.

The only thing I can conceive of that would be worse than this requirement would be if you proposed a constitutional amendment requiring a two-thirds popular vote or a two-thirds vote of the Electoral College to elect the President. It might literally be true, and history has proven this, that with such a requirement we would be unable to have a President, and that is the kind of straightjacket you are about to jump into and try on for size.

Madison—of course, this has been quoted very often by——

Senator BROWN. Let me ask you if I could—we are going to try and limit ourselves to 5 minutes.

Mr. CUTLER. Well, I will stop right there because everybody knows this Madison quote. Instead of having the majority decide what the country could do, subject only to the Bill of Rights and similar protections against even a willful majority, it would put the minority in power. The minority could block any kind of revision of the tax laws.

Senator BROWN. Thank you, Mr. Cutler. We will come back, I am sure, in questions. You have raised some important points. What we are trying to do is run the lights so that testimony is limited to about 5 minutes with it, and I have obviously not stuck with that, but we will try to do a little better as we go forward.

Senator BROWN. Now we will hear from a former colleague from Congress, a Member of the House of Representatives, a former Governor, Pete du Pont. We are pleased to have you here this morning.

STATEMENT OF PETE DU PONT

Mr. DU PONT. Mr. Chairman, thank you, and if I may have my entire statement submitted for the record, I will summarize my thoughts.

Senator BROWN. Without objection, the entire statement will be included in the record.

Mr. DU PONT. First of all, Mr. Chairman, it is the 15th of April and that reminds us of the language in the Declaration of Independence. One of the complaints that the American colonists had against King George was that "he has sent forth swarms of officers to harass our people and eat out their substance." The substance of every American family is being eaten out today by an over-bearing and over-reaching national Government that is taking far too much of their earnings in taxes.

I want to focus my testimony this morning on the experience in Delaware with a supermajority, an experience that I helped create and have watched for 16 years now. As a postscript, every one of Mr. Cutler's nightmares has, in fact, not come to pass in Delaware. There is no gridlock, as I will testify to in a moment.

First, though, three points. In 1909, a New York Times editorial said, and I quote, "When men get in the habit of helping themselves to the property of others, they cannot easily be cured of it." I would observe, exempting, of course, the people in this room on the distinguished panel, that the disease has only gotten worse, not better.

Ninety-eight percent of the families in the country didn't even pay the income tax when it began. On the other hand, it got to 90 percent under President Kennedy, and in 1990 President Bush and the Congress even agreed that it would require a supermajority of 60 Senators to cut taxes—an amendment, I am sure, much more favorable to Mr. Cutler's viewpoint—and a simple majority to raise them. I would say that the disease is progressing forthwith here in the U.S. Capitol.

In 1950, the average family was paying 3 percent of its income in Federal taxes. Today, the family is paying 25 percent. Our friend, Secretary of Labor Robert Reich, is fond of pointing out that over 20 years, from 1973 to 1993, the take-home pay of the lower two quintiles of the American economy, families in the lowest 40 percent income-earners in our country, did not see their incomes rise. In roughly that same 20-year period, the inflation-adjusted income of the Federal Government—that is, tax receipts—rose 58 percent. I would simply observe that there is fairness for you—working people, nothing; Government, plus 58.

But let me turn my attention to the States. One-third of all Americans, as Mr. Kemp said, live in States with tax limitations in their constitutions. Those with tax limitations saw slower revenue increases and slower spending increases than those without.

In our State of Delaware, the 1960's and 1970's exhibited all the problems that the Federal Government has here in Washington. On a bipartisan basis, Governors overspent State revenues. They were mostly thrown out of office by the voters for doing so. The first serious problem hit in the spring of 1969. Little after-shocks continued through 1975 and by the time I became Governor a year later, Republicans and Democrats agreed that it was time for both

a constitutional spending restraint and a second constitutional amendment limiting the ability of the legislature to increase taxes without a supermajority vote. I have attached the text of those two amendments to my testimony.

Since the constitutional amendments took effect in 1980, there have been 37 tax cuts enacted in Delaware and 23 tax increases. The taxpayers have won by a 3-to-2 margin. Most of the tax cuts were in personal income tax rates and gross receipts taxes. Most of the tax increases were in motor fuel taxes.

The personal income tax top rate started at 19.8 percent. It has now been reduced to 7.1 percent, a child care tax credit added, personal exemptions increased. Gross receipts taxes for businesses have been reduced every other year from 1985 to 1995. On the increase side, motor fuel taxes were raised in 1981, 1987, 1991, 1993, and 1995, and various other turnpike tolls, corporate franchise taxes and sin taxes raised as well. I should add that Delaware has no general sales tax.

So, what has been the experience in the Delaware economy over 16 years since 1980? Employment is up 39 percent, compared to 29 percent in the entire Nation. The unemployment rate has fallen by 49 percent; that is twice the drop in the national economy. AFDC caseloads are down 19 percent, compared to a 31-percent increase nationally. These two constitutional amendments led to a surge in economic growth. Personal income receipts have risen 26 percent, and so let me put that in perspective one more time. Top income tax rates have been cut 64 percent and income tax revenues are up 26 percent.

Mr. Chairman, in conclusion, I think a supermajority amendment is the only way that we are going to curb the spending and tax-increasing appetite of the Congress, and I have only one tongue-in-cheek suggestion to shortcut this process and get your amendment adopted more quickly, and that is to pass a simple statute today moving tax payment day from April 15 to October 15 so we would pay our taxes just before we vote. I think your amendment would sail through without any difficulty.

Thank you, Mr. Chairman.

Senator KYL. Mr. Chairman, might I comment? I have introduced a bill which would establish a commission to study whether moving tax day to the second Tuesday in November would be a good idea, and I would invite any of my colleagues to join in the cosponsorship of that legislation, a wonderful idea.

Senator BROWN. That is an excellent idea, but not known for a soft touch.

[The prepared statement of Mr. du Pont follows:]

PREPARED STATEMENT OF PETE DU PONT

DELAWARE'S SUCCESSFUL SUPERMAJORITY VOTE

Mr. Chairman and Members of the Committee: I am pleased to testify today in support of a constitutional amendment to require a supermajority vote in order to raise taxes, or increase or broaden the base or rate of existing taxes.

I bring to this question the perspective of a former state legislator, Member of Congress, and Governor of Delaware. In that last capacity, I supported and assisted the Delaware General Assembly (in Delaware the General Assembly has the exclusive power to amend the Constitution) in enacting an amendment to the Delaware

constitution requiring just such a super-majority vote. I want to focus my testimony on the success of that amendment in the 16 years of its operation.

First, however, I would like to state for the record, my belief that such a super-majority requirement is the only way that the revenue-raising impulses of the Congress will be controlled.

In 1909, a New York Times editorial opposing the income tax noted "when men get in the habit of helping themselves to the property of others, they cannot be easily cured of it." It is clear that they not only haven't been cured, their disease has gotten worse. The income tax that started so innocently in 1913 did not even apply to 98% of American families. By 1916, the top marginal rate had increased from 7% to 16%. By the '50s, it had risen to the confiscatory rate of 90%. Presidents Kennedy and Reagan each cut the top rate so that by the time Reagan left office, it stood at 33%, but it has inched up to over 40% again. By 1990, President Bush and the Congress would agree that a super-majority of 60 Senators be required to cut taxes, whereas a simple majority of 51 could increase them.

As Senator Roth, the Chairman of the Senate Finance Committee, has often pointed out, in the last few decades, every time Congress has raised taxes one dollar, it has raised spending $1.59, thus increasing pressure for further tax increases.

The problem has persisted since the end of the second World War. In 1950, the average family in America was paying 3% of its income in federal taxes. Today, that family is paying 25%. The value of the dependent deduction to median income families has been reduced by 75% since its enactment in 1946 by the failure of Congress to raise it to keep pace with inflation.

Secretary of Labor Robert Reich is fond of pointing out that from 1973 to 1993 the take-home pay of the lowest income 40% of American working men and women has in inflation-adjusted dollars remained flat. During roughly that same period, the inflation-adjusted income of the federal government has increased 58%. So the propensity to raise taxes has been a serious problem for working men and women for half a century.

Now let me turn to the experience of the states. One-third of all Americans live in a state with a tax limitation in their Constitution: Arizona, Arkansas, California, Colorado, Delaware, Florida, Louisiana, Mississippi, Oklahoma, and South Dakota. These provisions seem to have been effective, for as Congressman Joe Barton (R–TX) recently testified before the House Judiciary Committee Subcommittee on the Constitution:

> In the previous decade, taxes in nonsuper-majority states went up 104%. In super-majority requirement states, tax revenues went up only 87%. Tax limitation also slows growth in spending. In the same time period, spending in nonsuper-majority states went up 102%. In states with the super-majority protection, spending increased only 95%. So there has been both considerable experience and success at the state level in constitutionally limiting spending and taxation.

Turning to our experience in Delaware, during the 1960s and 1970s, the State of Delaware faced serious fiscal problems similar to those of the Congress in Washington. Our state government chronically overspent. Deficits became common. Tax increases the norm. Incidentally, this was a bipartisan problem; Democratic and Republican Governors both overspent the state's income. The first serious crisis hit in the spring of 1969 and its aftershocks continued through 1975.

Finally, in the late 1970s, Democrats and Republicans agreed it was time for both a constitutional spending restraint and a second constitutional amendment limiting the ability of the legislature to increase taxes without a super-majority vote. I have attached the texts of both amendments to my testimony and would like to submit them for the record.

Both amendments have been strongly supported by the general public and have operated successfully over 16 years, through three administrations of two political parties. They are not controversial, and I would venture the opinion that if anyone attempted to change them today, it would be met by solid public opposition.

The tax limitation is contained in two sections of Article VIII of the Delaware Constitution. Let me quote the operative sentences of Sections 10(a) and 11(a):

> Section 10(a)—The effective rate of any tax levied or license fee imposed by the state may not be increased except pursuant to an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House.
>
> Section 11(a)—No tax or license fee may be imposed or levied except pursuant to an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House.

Let me touch now on Delaware's experience with these two constitutional sections. First, since the effective dates of the amendments in 1980, there have been 37 tax

cuts and 23 tax increases; the taxpayers have won by a 3–2 margin. Most of the tax cuts were in personal income tax rates and gross receipts taxes. Most of the tax increases were motor fuel tax increases.

In Delaware, personal income tax rates in the 1970s were the highest in the nation, with a top rate of 19.8%. In 1980, 1985, 1986, 1987, and 1996, those rates were reduced. The top rate now stands at 7.1%. That is a 64% reduction in rates. In addition, various personal exemptions and pension deductions were increased and a child care tax credit added. Gross receipts taxes for businesses were reduced approximately every other year from 1985 to 1995.

On the increase side, motor fuel taxes were raised in 1981, 1987, 1991, 1993, and 1995. Turnpike tolls, corporate franchise taxes and alcoholic beverage and cigarette taxes were also increased from time to time.

I should add also for the record that Delaware has no general sales tax.

This pair of constitutional amendments has resulted in the adoption of fiscal policies that have benefited the individual taxpayer and produced surplus budgets for sixteen consecutive years. They have not throttled spending in Delaware. Indeed, spending increases in the General Fund have outpaced inflation in most of the years since 1985. But the climate of fiscal stability that these constitutional changes have brought to our state ushered in an era of unprecedented prosperity.

Since 1980, employment is up 39%, compared to 29% in the entire nation.

The unemployment rate has fallen by 49%, twice the national drop in unemployment.

AFDC caseloads are down approximately 19%, compared to a 31% increase nationally.

And as a result of this surge in economic growth, inflation-adjusted personal income tax receipts have increased 26%. Let me say that again: top income tax rates have been cut 64%, and income tax revenues are up 26%.

Unfortunately, like all states, Delaware suffers from rising federal income tax rates. Referring again to Secretary Reich's data, while inflation adjusted earnings in Delaware were falling 5% between 1975 and 1995, inflation adjusted federal income tax payments of the average Delaware family rose 17%.

In conclusion, super-majority constitutional amendments have corrected the recurring fiscal problems that Delaware was experiencing. They have created an economic climate of unprecedented prosperity. The rising tide of opportunity has lifted all boats. Now it is time for similar super-majority amendments to correct the unsuccessful fiscal policies the federal government has been following for the last half century.

tity in Chapter 97 (now Chapter 92) of Title 16, and therefore that section does not violate the pledge of credit provision of this section.

Wilmington Medical Ctr., Inc. v. Bradford, Del. Supr., 382 A.2d 1338 (1978).

§ 6. Procedure in withdrawal and payment of public moneys; annual publication of receipts and expenditures; limitation upon appropriations.

Section 6. (a) No money shall be drawn from the treasury but pursuant to an appropriation made by Act of the General Assembly; provided, however, that the compensation of the members of the General Assembly and all expenses connected with the session thereof may be paid out of the treasury pursuant to resolution in that behalf; a regular account of the receipts and expenditures of all public money shall be published annually.

(b) No appropriation, supplemental appropriation or budget act shall cause the aggregate State General Fund appropriations enacted for any given fiscal year to exceed 98 percent of the estimated State General Fund revenue for such fiscal year from all sources, including estimated unencumbered funds remaining at the end of the previous fiscal year. An act approved pursuant to § 3 of this article shall not be considered an appropriation for the purpose of this section. Estimated unencumbered funds are calculated by taking the estimated General Fund cash balance at the end of the fiscal year less estimated revenue anticipation bonds or notes, estimated encumbrances, estimated continuing appropriations and the amount of the Budget Reserve Account as established in subsection (d) of this section at the end of said fiscal year. The amount of said revenue estimate and estimated unencumbered funds remaining shall be determined by the most recent joint resolution approved from time to time by a majority of the members elected to each House of the General Assembly and signed by the Governor.

(c) Notwithstanding subsection (b) of this section, any portion of the amount between 98 and 100 percent of the estimated State General Fund revenue for any fiscal year as estimated in accordance with subsection (b) of this section may be appropriated in any given fiscal year in the event of emergencies involving the health, safety or welfare of the citizens of the State, such appropriations to be approved by three-fifths of the members elected to each House of the General Assembly.

(d) There is hereby established a Budget Reserve Account within the General Fund. Within 45 days after the end of any fiscal year, the excess of any unencumbered funds remaining from the said fiscal year shall be paid into the Budget Reserve Account, provided, however, that no such payment will be made which would increase the total of the Budget Reserve Account to more than 5 percent of only the estimated State General Fund revenues as set by subsection (b) of this section. The excess of any unencumbered funds shall be determined by subtracting from the actual unencumbered funds at the end of any fiscal year an amount which together with the latest estimated revenues is necessary to fund the ensuing fiscal year's General Fund budget including the required estimated General Fund supplemental and automatic appropriations for said ensuing fiscal year less estimated reversions. The General Assembly by a three-fifths vote of the members elected to each House, may appropriate from the Budget Reserve Account such additional sums as may be necessary to fund any unanticipated deficit in any given fiscal year or to

provide funds required as a result of any revenue reduction enacted by the General Assembly.

Cross references. — As to definition of terms used in this section, see § 6533(e) of Title 29.

Reviser's note. — The amendment to the Constitution set out above was initially approved as Chapter 609 of 61 Del. Laws on July 13, 1978, and finally approved as Chapter 234 of 62 Del. Laws on May 1, 1980.

Accounting for sources of revenue. — In order to comply with the constitutional mandate of this section, it is necessary for the General Assembly to be able to account for all sources of state revenue. Opinion of Justices, Del. Supr., 575 A.2d 1186 (1990).

"Money" in the "treasury" defined. — The words "money" in the "treasury," as used in this section, mean "money in the custody and control of the State Treasurer." Opinion of Justices, Del. Supr., 314 A.2d 580 (1974); Wilmington Medical Ctr., Inc. v. Bradford, Del. Supr., 382 A.2d 1338 (1978).

Terms include General Fund under 29 Del. C. § 6102. — The words "money" in the "treasury," as used in this section, include the General Fund as defined in 29 Del. C. § 6102. Opinion of Justices, Del. Supr., 315 A.2d 580 (1974).

§ 10. Limitation on increase of rate of taxes and license fees; exception to meet obligation under faith and credit pledge; allocation of public moneys to meet such obligation if revenues are not sufficient to meet such pledge.

Section 10. (a) The effective rate of any tax levied or license fee imposed by the State may not be increased except pursuant to an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House.

(b) Prior to the beginning of each fiscal year of the State, the General Assembly shall appropriate revenues of the State to pay interest on its debt to which it has pledged its faith and credit and which interest is payable in the year for which such appropriation is made and to pay the principal of such debt, payable in such year, whether at maturity or otherwise. To the extent that insufficient revenues of the State are available to pay principal of and interest on such debt when due and payable, the first public moneys of the State thereafter received shall be set aside and applied to the payment of the principal of and interest on such debt. To make up for such insufficient revenues, the General Assembly may increase the rate of taxes and fees without regard to the limitations of subsection (a) hereof after the failure to pay when due the principal of and interest on such debt.

Reviser's note. — The amendment to the Constitution set out above was initially approved as Chapter 510 of 61 Del. Laws on July 12, 1978, and finally approved as Chapter 234 of 62 Del. Laws on May 1, 1980.

Environmental permit fees. — This section requires an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House in order for the state to increase the environmental permit fees now charged and administered by the Department of Natural Resources and Environmental Control. Opinion of Justices, Del. Supr., 575 A.2d 1186 (1990).

§ 11. Imposition or levy of new taxes or license fees.

Section 11. (a) No tax or license fee may be imposed or levied except pursuant to an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House.

(b) Prior to the beginning of each fiscal year of the State, the General Assembly shall appropriate revenues of the State to pay interest on its debt to which it has pledged its faith and credit and which interest is payable in the year for which such appropriation is made and to pay the principal of such debt, payable in such year, whether at maturity or otherwise. To the extent that insufficient revenues of the State are available to pay principal of and interest on such debt when due and payable, the first public moneys of the State thereafter received shall be set aside and applied to the payment of the principal of and interest on such debt. To make up for such insufficient revenues, the General Assembly may increase the rate of taxes and fees without regard to the limitations of subsection (a) hereof after the failure to pay when due the principal of and interest on such debt.

(c) This amendment shall not apply to any tax or license fee authorized by an act of the General Assembly but not effective upon the effective date of this amendment

Reviser's note. — The amendment to the Constitution set out above was initially approved as Chapter 242 of 62 Del. Laws on May 18, 1980 and finally approved as Chapter 24 of 63 Del. Laws on May 28, 1981

Environmental permit fees. — This section requires an act of the General Assembly adopted with the concurrence of three-fifths of all members of each House in order for the state to impose fees for environmental permits currently issued without charge by the Department of Natural Resources and Environmental Control Opinion of Justices, Del Supr, 576 A.2d 1184 (1990)

Senator BROWN. We are joined by the House sponsor of this constitutional amendment, Congressman Joe Barton. Joe, you are welcome to join us up here, if you would like. Certainly, we would like to have Congressman Skaggs join us after he testifies, if he has time.

We are joined now at the witness table by a very distinguished Member of the House Appropriations Committee, Congressman David Skaggs from the great State of Colorado.

STATEMENT OF DAVID E. SKAGGS

Mr. SKAGGS. Good morning, Mr. Chairman. Let me thank you and the committee for the privilege of testifying today. I appreciate it greatly.

This proposed amendment, in my view, is a bad idea and bad constitutional law. Even worse, it will be considered today in the House of Representatives under a process that insults Members' intelligence and responsibility, contradicts any suggestion that the House might be a thoughtful body and, in fact, demeans and debases the very constitutional amendment process itself.

Second only perhaps to an act of Congress declaring war, an amendment to the Constitution ought to command the most serious and deliberate sort of legislative review, examination and analysis we are capable of. It deserves better treatment in the House than a rush job to meet a politically sexy vote deadline that the majority admits is a matter of symbolism. The Constitution should not be used to make political statements.

Each version of this proposed amendment has its own particular infirmities and I will address my remarks primarily to the proposal being considered in the House today. I oppose it on a number of grounds. It violates what Madison called the fundamental principle of free government, the principle of majority rule. The Constitution makes very few exceptions to that principle, none having to do with the core, ongoing responsibilities of Government.

I believe we should be extremely wary of any further exceptions, especially if it would complicate the essential responsibilities and competency of the Government. We have to be mindful that the logical corollary of supermajority rule is minority control, and under this proposed amendment 34 Senators, conceivably representing less than 10 percent of the American people, would have the power to control the Government's revenue and tax policy.

I also oppose this amendment because of its almost absurdly impractical consequences, both intended and unintended. One such consequence would be for all practical purposes to lock into law whatever was the then current tax structure at the time of this amendment's ratification. If you like the tax system the way it is now or if you have supreme confidence that some future Congress will have gotten it fixed just right before ratification, you should love this proposal. Another related consequence of this proposal would be to complicate efforts to balance the budget, particularly as they entail reducing the growth of entitlement programs. Finally, I am opposed to the amendment because, like the current House three-fifths rule, it is vague and will generate confusion and litigation.

Mr. Chairman, wiser lawmakers than we have considered the question of whether to require a supermajority for passage of certain kinds of legislation. At the Constitutional Convention, the Framers specifically considered and rejected proposals to require a supermajority to pass legislation concerning particular subjects, such as navigation and commerce. They rejected various legislative supermajority proposals largely because of their experience under the Articles of Confederation and the paralysis caused by the Articles' requirement of a supermajority to raise and spend money.

In other words, we have a Constitution because it was impossible for the country to function under a constitutional law such as is being proposed here. The Framers' judgment on this matter, including whether to retain the Articles' supermajority to raise revenues, should give us all cause to reflect on the wisdom of the proposals before the committee today.

In sum, this proposal would go far beyond any existing constitutional precedent. It would effectively paralyze the ability of future Congresses to deal with one of the most nuanced of all legislative issues—revenues and taxes—allowing a small minority to control national policy.

The Presidential primary election season brought forward a number of innovative ideas regarding the Federal tax system. Were it now in the Constitution, this amendment would likely serve to thwart these ideas or other reforms. Many want to end corporate welfare by closing tax loopholes, and that, of course, would likely bring in additional tax revenue from affected corporations and so require a two-thirds vote.

What about a capital gains tax cut? Its advocates usually argue that the effect will be to raise revenues. Does that mean the two-thirds requirement would kick in? If now in the Constitution, this proposed amendment would certainly make the current efforts to balance the budget a lot more difficult. Whether adjusting the Consumer Price Index or reducing business and tax subsidies, taxing the income of expatriates, limiting the use of section 936 credits in Puerto Rico, narrowing the EITC, means-testing Medicare Part B premiums, or limiting the amount of profits companies can shift to overseas subsidiaries, all would have to be passed by two-thirds. So once you consider how this amendment might be interpreted, many absurd consequences come to mind.

The short history accumulated on the application of the new House three-fifths rule is also instructive about the problems that would likely arise under this proposed amendment. In the 14 months that the three-fifths rule has been in effect, it has been waived 4 times. The amendments you are considering here, Mr. Chairman, are far more problematic because the Constitution can't be waived for convenience sake when questions arise.

One thing we can be sure of—we don't know the future. Why would we wish to deprive our successors in Congress of the tools and ability to deal with the problems they will face? To our successors, we are, in effect, saying we don't care what the particular circumstances may be in 10 or 50 years; we don't trust you and you are stuck with our expectations of your incompetence.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Skaggs follows:]

PREPARED STATEMENT OF DAVID E. SKAGGS

I want to thank the Chairman and the members of the Committee for the opportunity to testify today regarding a proposed amendment to the Constitution to require the vote of two-thirds of both houses of Congress to approve certain changes to federal revenue laws.

This proposed amendment is a bad idea and bad constitutional law. Even worse, it will today be considered in the House of Representatives under a process that insults Members' intelligence and responsibility, that contradicts any suggestion that the House is a thoughtful body, and that demeans and debases the very amendment process itself.

Mr. Chairman, let me say a word about the process that has brought this measure to the House today. The original proposal put forward by Representative Barton and Senator Kyl, H.J. Res. 159 and S.J. Res. 49, received one hearing in the House Committee on the Judiciary on March 6, 1996. It then was removed from that committee and scheduled for a vote on the floor. It was not marked up or approved by the Judiciary Committee. H.J. Res. 159 was then replaced by a second proposal, H.J. Res. 169, which is being considered today by the full House of Representatives. This version of the amendment was introduced on March 28, 1996, considered by the Rules Committee on March 29, 1996, and reported to the House. It has had no hearing at all in the committee of jurisdiction .

Second only, perhaps, to an act of Congress declaring war, an amendment to the Constitution ought to command the most serious and deliberate sort of legislative review, examination, and analysis we are capable of. It deserves better treatment than a rush job to meet a politically sexy vote deadline that the majority admits is a matter of symbolism. The Constitution shouldn't be used to make political statements.

I would, however, like to commend the sponsors of this bill on one point. They recognize that a change in the U.S. Constitution is necessary in order to require a super-majority to pass legislation on this subject. In effect, they concede that the attempt by the House in January, 1995 to simply pass a rule requiring a super-majority is not the proper procedure.

While each version of this proposed constitutional amendment has its own particular infirmities, I will address my remarks primarily to the proposal being considered by the House today (H.J. Res. 169).

I oppose this proposed constitutional amendment on a number of grounds. It violates what Madison called the fundamental principle of free government, the principle of majority rule. The Constitution makes very few exceptions to that principle, none having to do with the core, on-going responsibilities of government. We should be extremely wary of any further exceptions, especially if it would complicate the essential responsibilities and competency of the government.

We have to be mindful that the logical corollary of super-majority rule is minority control. And under this proposed amendment, 34 Senators representing less than 10% of the American people would have the power to control the government's revenue and tax policy.

I also oppose this proposed amendment because of its almost absurdly impractical consequences—intended and unintended.

One such consequence would be for all practical purposes to lock into law whatever was the then current tax structure at the time of this amendment's ratification. If you like the tax system the way it is now, or if you have supreme confidence that some future Congress will have gotten it fixed just right before ratification, you ought to love this proposal.

Another related consequence of this proposal would be to complicate efforts to balance the budget, particularly as they entail reducing the growth of entitlement programs.

Finally, I'm opposed to this proposed amendment because, like the current House three-fifths rule, it is vague and will generate confusion and litigation.

I know the authors of this proposal feel strongly about taxes. But simply having strong feelings about an issue is not sufficient reason to cede power over all future changes to an important area of national law to a small minority. In addition to the tax issue, Members of Congress will typically have very strong feelings on a number of issues—civil rights or trade or the deployment of U.S. troops abroad. In none of these areas does it serve the long-term national interest to undermine the principle of majority rule. In short, my opposition to this proposal is primarily grounded in the fundamental principle that is at stake, the principle of majority rule—the fundamental principle of free government.

Wiser lawmakers than we have considered the question of whether to require a super-majority for passage of certain kinds of legislation. At the Constitutional Con-

vention, the Framers of the Constitution specifically considered—and rejected—proposals to require a super-majority to pass legislation concerning particular subjects such as navigation and commerce. They rejected various legislative super-majority proposals largely because of their experience under the Articles of Confederation and the paralysis caused by the Articles' requirement of a super-majority to raise and spend money. In other words, we have a Constitution because it was impossible for the country to function under a constitutional law such as is being proposed here.

The Framers' judgment on this matter, including whether to retain the Articles' super-majority to raise revenues, should give us all cause to reflect on the wisdom of the proposals before the Committee today.

In those cases in which the Framers did impose super-majority requirements, none deals with topics of regular legislative business central to the on-going operation and management of federal government, such as taxes and revenues.

In those cases in which the Framers did impose super-majority requirements, only two require action by both bodies, namely, the override of a presidential veto and the referral of a proposed amendment to the states. Both are extraordinary matters.

In sum, this proposal would go far beyond any existing constitutional precedent. It would effectively paralyze the ability of future Congresses to deal with one of the most nuanced of all legislative issues—revenues and taxes, allowing a small minority to control national policy.

The presidential primary election season brought forward a number of innovative ideas regarding the federal tax system. Were it now in the Constitution, this new amendment would likely serve to thwart these ideas or other reforms. This amendment would certainly apply to flat tax proposals which proponents claim would increase economic growth and, therefore, federal revenues. This proposed amendment would likely require a two-thirds vote on legislation implementing the consumption tax or Value Added Tax (VAT) proposed by some, which again proponents believe would increase economic activity and federal revenues. There's been a lot of talk on both sides of the aisle about getting rid of corporate welfare. Many want to end corporate welfare by closing tax loopholes—and that, of course, would likely bring in additional tax revenue from affected corporations and so would require a two-thirds vote under this proposal. And what about capital gains tax cut? Its advocates usually argue the effect will be to raise revenue. Does that mean the two-thirds requirement would kick in?

But let's say we tried one of these ideas out before the amendment took effect. Is anyone certain enough that one of them is the correct solution to the tax reform problem that you wish to make repeal or revision next to impossible?

And if this proposed amendment were part of the Constitution, it would probably make it more difficult to reduce taxes. If at some point in the future, Congress judges the budget and economy healthy enough to reduce taxes, how likely is it that a responsible Congress would go ahead and do so knowing that it would be almost impossible to raise rates again in the event circumstance required it?

If now in the Constitution, this proposed amendment would certainly make the current efforts to balance the budget a lot more difficult. Whether adjusting the Consumer Price Index (CPI), or reducing business and tax subsidies, or taxing the income of expatriates, or limiting the use of section 936 tax credits for business activities in Puerto Rico, or narrowing the EITC, or means testing Medicare Part B premiums, or limiting the amount of profits companies can shift to overseas subsidiaries—all would have to be passed by two-thirds.

It is important to realize that the proposal being considered by the House today is not a really a tax amendment at all. The word 'tax' does not appear in the text, nor does 'income tax,' 'tax rate,' or 'new tax.' It is a "revenue" amendment. The only legislation requiring a two-thirds vote under this proposal is that which has the effect of increasing "internal revenues."

There is no technical definition of "internal revenues" except perhaps as distinguished from revenues from "external" sources, such as import duties. All other sources of federal revenue are presumably included under this proposed amendment. So any legislation to increase any federal fee or charge or fine would be subject to a two-thirds vote if it results in more than a "de minimis" increase in revenues. So would any proposal to sell federal assets—another frequent component of budget-balancing and privatization plans. And according to the proposed amendment, "de minimis" is to be defined by Congress at some later time. Or quite conceivable, at each time a revenue bill is considered, inviting an exercise in manipulative definition whenever the prospect of winning two-thirds approval was dim.

On the other hand, it's arguable that this proposal would not necessarily require approval of two-thirds for a tax increase. Some tax increases can actually reduce or, at least, not increase revenues. For example, the luxury tax on certain boats and

cars that was repealed in 1993 is said to have actually reduced sales so dramatically that associated revenues actually declined. Some even argue that most tax increases on business activity actually reduce federal revenues by depressing economic growth. What economic theory, interpreted by which expert, will therefore determine the application and effect of this amendment if it were adopted?

So, once you consider how this amendment might be interpreted, many absurd consequences come to mind.

In the context of deficit reduction, we should also consider the fairness and equity implications of this amendment. Most federal benefits to lower and middle income Americans come from programs that depend on direct expenditures. The benefits of upper income Americans and corporations often come through various kinds of tax breaks. since this amendment would require a simple majority to cut programs benefiting lower and middle income Americans, but a super-majority to reduce tax benefits to wealthy Americans and corporations, it would unfairly bias deficit reduction and create a path of least resistance that would disproportionately hurt middle and lower income citizens.

Of course, it is to examine and understand exactly these sorts of things that we usually refer legislation, especially amendments to the Constitution, to committee. There, these and other questions can be asked and answered and necessary refinements and revisions to a proposal can be crafted. Sadly, no, shamefully none of this regular order has been followed in the House.

In evaluating this proposed amendment, it's also helpful to examine some recent experience in the House. In the 104th Congress, the House pretended to operate under a new rule requiring a three-fifths vote to pass any increase in a Federal income tax rate. Obviously, the amendments before the Committee today would go much further.

The short history accumulated on the application of the new House rule is instructive about the problems that would likely arise under this proposed constitutional amendment. In the 14 months that the three-fifths rule has been in effect, it has been waived during consideration of the majority party's Budget Reconciliation bill (H.R. 2491), the Contract with American tax bill (H.R. 1215), the majority's Medicare bill (H.R. 2425), and, recently, the House version of the Kennedy/Kassebaum health care bill (H.R. 3103). These waivers have been accompanied by dispute and confusion as to the meaning of the rule.

The amendments you are considering, Mr. Chairman, are far more problematic because the Constitution can't be waived for convenience sake when questions arise. And you can be certain that similar questions about the meaning of this amendment will arise in great number. The net effect would probably be for almost any future tax bill that passed by less than two-thirds under some claimed exemption from this amendment to be subject to protracted litigation, creating an outcome we ought to avoid in tax law—uncertainty and confusion.

Much of the criticism I've offered about the amendment being voted on today in the House (H.J. Res. 169) can also be made of the original version (S.J. Res. 49–H.J. Res. 159), which addresses any "new tax or increase in a tax rate or base," as opposed to an increase in "internal revenues." While the original version directly addresses the issue of taxes, instead of the vague concept of "internal revenue," it would also obstruct many proposed approaches to tax reform and interfere with efforts to balance the budget. It would require a two-thirds vote on flat tax proposals which would increase the tax base as they reduce the tax rate, on legislation implementing the new consumption tax or value added tax (VAT) proposed by some members of Congress, and on closing tax loopholes that also necessarily increase the tax base. Instructively, if the original version of the proposed amendment were already a part of the Constitution, the new majority in this Congress could not have passed its budget bill, which effectively increased taxes on Americans eligible for the Earned Income Tax Credit.

In those cases in which the Framers did impose super-majority requirements, or any voting requirement, none is based on the full membership of the body, as opposed to those present and voting. The original version of this proposal requires two-thirds of the membership of both houses of Congress. By requiring two-thirds of the membership, this proposal would make it more difficult to close corporate tax loopholes than to remove the President of the United States from office under Article I, sec. 3, cl. 6 of the U.S. Constitution.

One thing we can be sure of. We don't know the future. Why would we wish to deprive our successors in Congress of the tools and ability to deal with the problems they will face? To our successors we are in effect saying, "We don't care what the particular circumstances may be in 10 or 50 years; we don't trust you, and you're stuck with our expectations of your incompetence." What arrogance!

Mr. Chairman. I urge you and the members of the Committee to take a close look at this proposed constitutional amendment in the light of the wisdom and experience of the Framers, its stifling and absurd effects, and the history of the House of Representatives' 3/5ths rule. Treat it for what it is, a political statement—and one better made on the floor of the Senate or House than put into the U.S. Constitution.

Senator BROWN. Thank you. You have raised some important points. I know we will want to cover them with questions afterwards.

Congressman Barton, you have been kind enough to join us. Do you have a statement you would like to add to our deliberations?

STATEMENT OF JOE BARTON

Mr. BARTON. I will do it in less than 5 minutes, Mr. Chairman.

First, let me thank you for allowing me to testify with this distinguished panel. When you have counselors to the President, former Cabinet Secretaries, former Congressmen and Governors and, of course, my colleague, David Skaggs, who is known as one of the most intelligent, intellectual Members of the House, it truly is a privilege.

I want to comment very quickly on some of the points that Congressman Skaggs raised. In 1787 when we adopted the current Constitution, I am not aware that there was an income tax being levied anywhere in the world and the reason there was not is that at that point in time, most of the world's economy was still agrarian and based on barter and so there weren't large incomes to be taxed.

Even then, the Founding Fathers realized that raising taxes was a proposition that should be done carefully and they gave to the House of Representatives that we elected by the people directly—the only Federal office-holders directly elected by the people—the power to introduce the tax laws, and they felt that was sufficient protection.

In the original Constitution, there were a number of instances, though, that the Founding Fathers required supermajorities to ratify treaties, to amend the Constitution, to expel a Member, to impeach a sitting Federal judge, and so on. The reason that you have supermajorities is because you want consensus. You don't want a slim majority acting in the heat of the moment to pass things that fundamentally alter future generations.

I am very confident that had we had income taxes being levied in the 1780's and if income taxation was the fundamental way that the Federal Government was going to raise revenue, it would have required a supermajority vote in 1787. Having said that, in 1913 we passed the Sixteenth Amendment to the Constitution that said the Federal Government directly had the authority to levy an income tax. The first income tax was 1 percent on income up to $20,000. That was called the normal tax, and then you paid an additional 1 percent on up until finally you paid 6 percent on income over, I believe, $800,000.

Since 1913, the marginal tax rate on the average American taxpayer has risen 4,000 percent, 4,000; that is a four and three zeroes, 4,000, since 1913. At some point in time, the American people are going to say enough is enough, and all of the Washington-in-

sider arguments about being pragmatic and all of that simply is not going to wash.

There are 10 States that have some form of supermajority requirement to raise taxes on their books right now. Not one State that has implemented it has repealed it, not one, and the reason is it works. Taxes are lower and they go up slower in States that have some form of tax limitation amendment. In States that don't, taxes are higher and the taxpayer's pocketbook is left drier. So it boils down to are you for lower and slower or higher and drier, and I am for lower and slower—lower taxes going up more slowly.

So when we vote on the House floor this evening about 9 p.m., the Congressmen that are here today and voting have got a clear choice. They can vote for tax limitation that has been proven to work in the States that have it or they can vote against it, and if they vote against it, then they can go to their constituents in the election next fall and explain why they voted not to require the supermajority and they may be able to explain it and they may be able to get their constituents to agree with them.

But in Texas, in my district, in the last year when I have been talking about this, I have not had one constituent tell me to vote against tax limitation because as we speak today, Mr. Chairman, there are people in my district and your State that are literally working second jobs, part-time jobs, so that they have enough money in the bank when they write the check tonight before midnight to send to the IRS that they know that check won't bounce.

This tax limitation amendment is not for you and it is not for me and it is not for the people at this table. It is for the average American taxpayer who is simply trying to make ends meet and do for their families so that the Government does not have to. So if we don't pass it tonight, it is going to come back. We are like Freddie in "Friday the 13th" movies. If we don't get it tonight, we are going to come back every April 15 that the Republicans are in control of the House of Representatives and we will keep voting on this amendment until we do get the two-thirds vote, and hopefully the Senate the same, and send it to the States for ratification.

Thank you, Mr. Chairman.

Senator BROWN. Thank you.

Senator Kyl, do you have questions?

Senator KYL. Yes, I do. First of all, let me thank all of the witnesses for very fine statements. I am going to start with Mr. Cutler because I think that the technical arguments that you raised against the amendment are the appropriate technical arguments. I would suggest that they are technical and that they don't establish a strong enough case against the amendment, considering the rationale for it as expressed by Governor du Pont and Secretary Kemp. That is my own personal view, but I would like to break your points down into four specific categories which I think represent the essence of your argument, Mr. Cutler.

Your first point was that this amendment would create a straightjacket; that even if a majority of the people believe that we should have tax increases, it would make it harder to enact them. Of course, it would make it harder to raise taxes, and you cited an example of a military conflict which didn't rise to the level of a

war, but clearly would be a situation in which we may need to raise revenue.

Now, first, I would ask—you may be aware that there are several polls, including a Reader's Digest poll, which point out that between 68 and 70 percent of the American people think they are taxed too much and oppose the latest tax increase. I am talking about the 1993 tax increase. So it is hard to believe that a majority of Americans agreed with that tax increase in 1993.

Do you have any evidence that the tax increases that have been most recently passed are supported by a majority of the American people?

Mr. CUTLER. Well, we live in a representative form of Government. We elect Members of the House and the Senate. We now have substantial Republican majorities in both the House and the Senate. If you think taxes are too high and that the public thinks taxes are too high, why don't you pass bills lowering them?

The gist of this amendment appears to be you are going to have your majority for such a short period of time, you must protect yourself against the majority that will come along in the future and feel it necessary, because of some emergency, to raise a tax.

Senator KYL. I would just like to respond that I think the elections of 1994 were the result of the American people's disgust at the 1993 tax increase——

Mr. CUTLER. Then why don't you pass a bill?

Senator KYL [continuing]. Where they threw out the democratic majority that was responsible for passing it and for the first time in 40 years elected a Republican House of Representatives and a Republican Senate. The change in leadership was largely in response to that tax increase. It hasn't yet gotten the tax increase wiped off the books and that is a problem.

Mr. CUTLER. But you have the majorities that can do it.

Senator KYL. Well, unfortunately, we have a President that vetoed our Balanced Budget Act.

Mr. CUTLER. Then why don't you introduce a constitutional amendment saying that a veto can be overridden by a simple majority? That makes more sense than what you are actually proposing here.

Senator KYL. I don't favor that.

Secretary Kemp.

Mr. KEMP. The Congress, Lloyd, has cut taxes several times and in each case, both for families, for moderate-income people and workers, and on capital gains—every time, the President has vetoed it.

Mr. CUTLER. Then elect a President, for God's sake.

Mr. KEMP. The President is frustrating the will of the majority.

Mr. CUTLER. Elect a President.

Mr. KEMP. This is not the issue, this is not the issue. This amendment that has been alluded to by both Jon Kyl of Arizona and Joe Barton of Texas is aimed not at the next Congress. It is aimed at our posterity. It is aimed at the next century. It is aimed at once we get in place a new tax system that there be a fundamental respect for the system that is not changed at midnight and not changed by circuitous and surreptitious means to try to take the substance, as Joe Barton put it, from the American people.

Excuse me, Jon. I appreciate your letting me make that comment, but you had another question.

Senator KYL. We are under the 5-minute rule, right, Mr. Chairman?

The CHAIRMAN. I think we are trying to do 7 minutes. If we have new members come, we may need to shorten it.

Senator KYL. As long as the witnesses understand we are under a 5-minute rule, I won't filibuster if you won't. Thank you.

The second point that you made, Mr. Cutler, was that the ticket tax on airline tickets expired not by intent but as a result of budget gridlock. I am not sure that is an accurate characterization, but I know what you mean and I guess what I would suggest is that if it was a mistake, if we really didn't mean for it to expire, it shouldn't be too hard to get two-thirds to agree to reinstate it. I wouldn't think.

Mr. CUTLER. You can get a majority to do it right now. Why aren't you doing it? The President is not going to veto that.

Senator KYL. Well, that is a very good question. Maybe it wasn't by mistake, then.

Third, Members could just absent themselves. That is correct, but now that I have been a Member of both the House and the Senate, one of the things I've learned is that one of the last things Members want to do is not be recorded on a vote. I mean, voting for or against, you can at least take your stand, but being a chicken and not voting at all is probably the worst of all.

In my entire 10 years in the U.S. Congress, there has only been one incident where Members decided to withhold their votes and they voted "present" rather than voting for or against, and they certainly never absented themselves. I doubt that that is a serious objection. Any of the House Members may want to comment on that, but I really don't think it is that serious.

Mr. BARTON. Well, in a constitutional amendment, if you vote "present," it basically counts as a no vote.

Senator KYL. As Mr. Cutler pointed out.

Mr. CUTLER. Well, I just wanted to point out that the House bill does not do what your bill does, Senator Kyl. The House bill is two-thirds of those present and voting.

Senator KYL. That is correct, and we are talking specifically here about the Senate bill, but next time I have an opportunity to ask questions, I probably will ask some of you the difference between the House and the Senate bill.

Mr. CUTLER. I would just make one other comment.

Senator KYL. Yes.

Mr. CUTLER. Secretary Kemp was talking about the aim of this amendment. The aim of the amendment, as I see it, is no matter whom a majority of American citizens elect as their President and no matter whom they elect to Congress, a majority cannot be trusted and the President cannot be trusted on the issue of tax cuts.

Senator KYL. Well, Mr. Cutler, if you want to characterize it that way, then the Framers were of the opinion that a majority couldn't be trusted to amend the Constitution because it requires a two-thirds vote of both the House and Senate and three-fourths of all the States. Were they saying that the majority couldn't be trusted?

No. That is a facetious argument. What they were saying is there are some things that are so important that a consensus more than the mere majority is required.

James Madison was one of the people who was quoted here. Let me tell you what James Madison said. I think Representative Skaggs quoted Madison. I am not sure I have it right here at my fingertips, but he talked about the need to control a runaway majority, and that is one of the reasons why we have several provisions both in our Constitution and also in the rules of the House and Senate that require us sometimes to slow down, think it over, and develop a consensus because the issue is so important. To ratify a treaty, for example—that shouldn't be done just lightly. It is not that we don't trust the majority. It is that it is too important just to have a majority vote.

Mr. CUTLER. That is the issue. It is whether you want to embody in the Constitution a requirement of this rigorous two-thirds majority which you may need to change some time and you cannot form the necessary two-thirds majority, plus three-quarters of the States to change it. That is what I meant by the straightjacket.

Senator KYL. That is a fair way to state the issue.

Mr. KEMP. Even the President, if I may interject, said in Houston not so long ago that he raised taxes by mistake. He said he was tired and it was late at night, and he apologized to a Houston fundraiser of the Democratic Party for raising taxes and he got into all sorts of problems.

Now, maybe, had there been a two-thirds majority, he might not have made such a mistake. He is trying to do it again. He is saying that capital gains are too low; we should raise them again. We have the only unindexed capital gains tax that I know of in the industrial world and it is the confiscation of the wealth of the people of this country, as Congressman Barton talked about, that was not envisioned by the Founders.

We have heard from James Madison here both implicitly and explicitly. My favorite Madison quote is when he said at the ratification of the American Constitution, we have staked the whole future of American civilization not upon the capacity of government, but upon the capacity of people. The future of America is based, he said, upon the future of people to be able to sustain themselves under the Ten Commandments of God.

I would make a case that Barton and du Pont and you, Mr. Chairman, and you have made several times, Senator Kyl, that we are making it impossible for the American family to sustain themselves in a free society by confiscating their property, their earnings, their salaries, their savings, their investment, and it has to be changed. In my opinion, I was somewhat trepidatious about appearing here today on behalf of an amendment until we had passed comprehensive tax reform such as envisioned by the commission appointed by Bob Dole and Newt Gingrich. But after listening to Mr. Cutler, counselor Cutler, and my friend, Dave Skaggs, I am absolutely convinced that this is a necessity going into the eve of the 21st century.

Thank you, Mr. Chairman.

Mr. BARTON. Mr. Chairman, could I just read the quote that Senator Kyl——

Senator KYL. Federalist 51?
Mr. BARTON. Yes.
Senator KYL. Yes.
Mr. BARTON. If you want to read it, I have got it.
Senator KYL. Well, thank you. Mr. Chairman, just for the record, in Federalist 51 Madison said, "It is of great importance in a republic not only to guard the society against the oppression of its rulers, but to guard one part of the society against the injustice of the other part." He didn't specifically speak in terms of majority rule, but it was in the context that he made the statement.
Senator BROWN. Thank you. Mr. Cutler, you are known to be very thoughtful and wise, and your review of the motives of the people involved here, I fear, may well be correct. It is one of those things that sometimes we hope the witnesses aren't always wise or always right.
One of the things you raised, though, that I thought was a very important point was the suggestion that this could result in gridlock; literally, to put it a different way, that we would not be able to pass a tax increase when perhaps it was appropriate, albeit the various parties have different views as to when it is appropriate, some of us much less often than others, but fair enough.
I look back, though, through the tax increases since 1980 and, as you know, there have been a number of them, but of the ones that would be major—that is an arbitrary description, but of the ones that are major—of those 13, 7 of them did have a two-thirds majority of both Houses and 6 of them did not. Does that change your thinking? I mean, is your thought that perhaps the people who had voted for it if they had had a chance to defeat it would not have voted for it?
Mr. CUTLER. No, it doesn't change my thinking, especially if it comes out seven to six, as you have said, because it is in the case of the six that you need to do something and you are blocked from doing it, except by an amendment process which takes—even for successful amendments, usually takes about 7 years. That is the problem.
Senator I am not an opponent of lowering taxes, eliminating the capital gains tax or any of those things. I do have the view of the Concord Coalition that budget deficit reduction is so important it cannot be accomplished, or may not be accomplishable solely by reducing expenditures. There may be times when we cannot reduce expenditures, such as the new military threat that I referred to which has not yet resulted in any kind of armed conflict.
Senator BROWN. I understand.
Mr. CUTLER. You just don't have enough outs. You don't have enough escapes in this. Even in the balance-the-budget amendment, when it had a limit on tax increases, there were outs. Congress could excuse itself in some sort of emergency. This is a no ifs, ands, or buts amendment.
Mr. BARTON. That is not true, Mr. Chairman.
Senator BROWN. Let me go ahead. We are down to 7 minutes and I want to try and get through a couple additional questions.
Governor du Pont, for most of my political lifetime I have always heard tax increases described as a tax on someone else—a tax on the very wealthy, a tax on a different part of the country. New

taxes have been sold oftentimes as taxes that won't hit your voters, but someone else's voters.

We are now at a point where about 40 percent of the GDP goes to government taxes. We are committed as a society to exempting about a third of our citizens from taxes, certainly from income taxes. The exemption runs a little higher than that in terms of any subsidy of taxes. Who is going to pay tax increases from this point forward, the wealthy or the average working person?

Mr. DU PONT. Well, of course, Mr. Chairman, the current tax code is well publicized as a tax on the wealthy, but it has quickly eaten out the substance of the middle class, and as Secretary Kemp testified a few moments ago, the wealthy always manage to pay about the same share regardless of rates. It didn't seem to matter whether the rate was 91 or 26. The share of GNP in the economy going to taxes remains approximately the same.

But I would like to respond to Mr. Cutler that he makes it sound as if, with a two-thirds margin, supermajority, no one will ever pass a tax increase again. I happen to think that is a wonderful outcome, but I don't think that that is true. Twenty-three times, the Delaware Legislature managed to pass tax increases in 16 years, most of them broad-based—cigarette taxes, gasoline taxes, turnpike tolls, and so forth. They achieved a supermajority without difficulty.

If a military threat from China came, I imagine you would see the entire conservative contingent in the House voting for a tax increase to meet that threat. It just seems to me it makes it a little more difficult, but he makes it sound that we are never going to pass a tax increase again, and that is certainly not the experience of these 10 States who have adopted constitutional amendments.

Senator BROWN. Thank you. Congressman Skaggs, you raised a very important point about the extent of the language and how the amendment, the way it is drafted, could even require a two-thirds majority to reduce taxes. I think your specific example was capital gains.

In looking at the language of the Kyl amendment, it says, "Any bill to levy a new tax"—obviously, a reduction in capital gains would not be a new tax—"or increase the rate"—and that wouldn't apply to a reduction in capital gains—"or base"—and I don't think that would apply, but perhaps you have a different interpretation of those words.

Mr. SKAGGS. Mr. Chairman, my remark was addressed to the language of the House proposal which we will vote on today, which speaks in terms of raising internal revenue. So if, as is argued by many proponents of the capital gains tax cut, it will ultimately raise revenue, then we are in the ironic situation under the House proposal in which it might take two-thirds to cut a tax rate because it would have the effect—according to the advocates of a capital gains tax cut, it would have the effect of raising revenue. I believe Mr. Kemp is a particularly strong supporter of that school of economics.

Senator BROWN. You are going to make us live with that rhetoric about lower taxes resulting in greater revenue.

Mr. SKAGGS. Joe's colleague and mine, Dave Dreier, had some very serious reservations about this expressed when the Rules Committee rushed this matter to judgment a couple of weeks ago.

Mr. BARTON. Could I respond to that?

Senator BROWN. Surely.

Mr. BARTON. Well, quickly, first of all, under current scoring rules of the House and the Senate capital gains are revenue losers, so you don't have the problem that Congressman Skaggs talked about. But in the real world, I agree with him. If you cut capital gains, you probably would raise revenue and I am willing to live with that.

Under our rules, what it would mean is we would have to cut another tax rate. What is wrong with that? I mean, you can't get around it. If you want to cut capital gains, either way under current scoring it loses revenue, so there is not a two-thirds requirement. You can do that by majority. But if you assume dynamic scoring and it is going to raise revenues, fine. Let's cut another tax rate at the same time so that the overall effect of revenue neutrality and you get the best of both worlds.

Mr. SKAGGS. Mr. Chairman, just one further observation. I think Mr. Barton's response underscores another very problematic aspect of this proposal, and that is subjecting the interpretation of the Constitution, were this to be in the Constitution, to particular economic theories or schools of thought or definitional manipulations. Is that really the sort of question we wish to beg in amending the Constitution of the United States?

Mr. BARTON. Everything that is in the Constitution, whether in the original or amended, is subject to implementation language by legislation.

Senator BROWN. Let me thank the panel. Let me thank particularly the two Congressmen that have joined us, and I would extend an invitation that if they would like to join us up here for the deliberations, we would love to have them.

Senator KYL. Mr. Chairman, as a point of personal privilege, might I ask Mr. Cutler one final question? I have used the quotation, "Reform? Sir, don't talk of reform. Things are bad enough already." I thought it was in *A Tale of Two Cities,* by Dickens—not there, and I have sought in vain for years to find the source. You appear to have the source of that statement. Would you tell me what that is again?

Mr. CUTLER. I think I recently read it in Roy Jenkins' biography of Gladstone, but I will find it for you.

Senator KYL. Would you please do that? I would love to be able to—it is a wonderful quotation which fits many occasions.

Mr. CUTLER. Mr. Chairman, I didn't answer Governor du Pont's point which he made twice about how all these prophecies of doom did not occur in the State of Delaware. I just want to say the State of Delaware is not responsible for the national defense. It is not responsible for budget deficit management at the Federal level and it is not responsible for broad economic policy and economic growth at the Federal level.

I have no doubt myself, knowing Governor du Pont's abilities, that if he didn't have that two-thirds requirement in the State of

Delaware, his personal appeal would have gotten through almost everything he accomplished.

Mr. DU PONT. You know, Mr. Chairman, this hearing has gone too long. [Laughter.]

Senator BROWN. Thank you all.

Mr. KEMP. Thank you. Thank you, Mr. Chairman.

Senator BROWN. Our second panel will come forward. It includes John McGinnis, who is a professor of law at Cardozo Law School in New York, and David Strauss, a professor of law at the University of Chicago School of Law. Gentlemen, thank you for joining us.

Professor McGinnis, perhaps you might start us off.

PANEL CONSISTING OF JOHN O. McGINNIS, PROFESSOR OF LAW, BENJAMIN N. CARDOZO SCHOOL OF LAW, NEW YORK, NY; AND DAVID STRAUSS, PROFESSOR OF LAW, UNIVERSITY OF CHICAGO SCHOOL OF LAW, CHICAGO, IL

STATEMENT OF JOHN O. McGINNIS

Mr. MCGINNIS. Yes. Thank you very much, Senator. I am delighted to be here and I would ask that my written remarks be put in the record. I will testify here orally about the concept of why we need a supermajority for raising taxes. I am not going to go into the details of either Senator Kyl's amendment, which I have gone into in my written testimony, or of Congressman Barton's, but I would be happy to answer questions about that and I would be happy to work with your staff about that.

There are two reasons, I think, that the concept of a supermajority amendment to raise taxes is really crucial and why we need to seize this historic opportunity at the moment. The first is that such an amendment will reduce the disproportionate power of concentrated interest groups in our republic, and the second is that it will restore the Framers' protections which have been weakened over the years for the rights of property and enterprise.

Let me begin with the problem of concentrated interest groups. The Framers well understood that a legislative majority was not necessarily a popular majority, and that is even clearer in modern democratic theory. Public choice theory shows why concentrated interest groups have more power than diffuse interest groups, diffuse interest groups here meaning the average citizen, concentrated interest groups meaning some group that has some ability to lobby the legislature because they can gain specific benefits from it.

Because of the disproportionate power of concentrated interest groups, legislatures often have an agenda of giving entitlements or specific benefits to those groups, while diffusing the costs on the average citizen in the form of taxes. In many ways, our current budget deficit and our current very high tax rates are an instance of that repeated dynamic of an agreement to give benefits to concentrated interest groups while diffusing the costs and therefore making it harder for legislatures to be held accountable for their actions. So, that is the first reason that it would be very important to pass a supermajority requirement.

The second reason is that it protects human liberty. It is wrong to think that the Framers instituted a pure democracy or pure majoritarian rule. They were very specific. They instituted a repub-

lic to protect certain liberties. Indeed, James Madison, who has been quoted here, said the first object of the republic is to protect the different abilities to acquire property. The rights of property and enterprise were central to our original Constitution and they were protected in a variety of ways, including property rights—the Takings Clause or the Contract Clause.

Throughout the whole structure of the Constitution was an idea of protecting property. The right of federalism was intimately connected to property rights. The idea there was that you allowed a great power, a substantial power to the States because a national citizenry had the ability to move away from an oppressive state. Federalism was a protection against leviathan.

Finally, the separation of powers was a protection of individual liberty. Indeed, the purpose of it in some sense was to ensure a bit of gridlock in Government. It would make it harder to impose regulations and other burdens on citizens.

The difficulty is that, for a variety of reasons in the past 50 years, these protections for the rights of enterprise and property have been substantially weakened. We should not think, therefore, of this amendment as some radical innovation, but really as a way of restoring the Framers' vision of the Constitution which had as its core the protection of these rights of property and enterprise. Those, I think, are the two reasons that we should be supporting this amendment.

First, contrary to the opponents of the amendment, it actually helps popular majority by reducing the power of concentrated interest groups and giving power back to the average citizen who pays taxes but isn't really very good at lobbying the legislature; second, by restoring the essential republican right, one of the many important rights of the republic, but probably the most essential to the Framers, the rights of property and enterprise.

Thank you, Senator.

Senator BROWN. Thank you, professor.

[The prepared statement of Mr. McGinnis follows:]

PREPARED STATEMENT OF JOHN O. MCGINNIS

Thank you very much for the opportunity to testify today in support of the concept of a constitutional amendment that would require a supermajority to raise taxes. We will offer two major arguments in favor of a supermajority taxation amendment in the abstract and then offer some brief thoughts about the S.J. Res. 49, the draft of such a constitutional amendment that is before us. We stress that our primary focus here is to support the concept of a supermajority requirement for raising taxes. It would be a great mistake to allow arguments about details to make us miss this historic opportunity. We would be very pleased, however, to work with your committee's staff as this amendment moves through the legislative process. It would be a pleasure to participate in such an important enterprise.

A constitutional amendment to require a supermajority to raise taxes will help correct the major problem of contemporary politics—the ability of concentrated interest groups to obtain programs that benefit themselves at the expense of a diffuse and relatively helpless public. Second, such an amendment would also help restore the original Constitution's delicate balance between structures that protect individual rights and ensure economic growth and those that promote democratic governance. Thus we believe that a supermajority taxation amendment should be seen as an attempt to revive the original values of the Constitution rather than as a radical innovation.

The objective of the original Constitution was to establish a well functioning republic—a concept which is not necessarily synonymous with government by a simple legislative majority on all issues. The Framers well understood that a legislative

majority only imperfectly reflected the majoritarian will of the people as a whole.[1] Moreover, the Constitution was designed to optimize the protection of the people's individual rights as well their political rights. In our republic deliberative democracy is not the entire end of government but is also a means for advancing human liberties.[2] The Constitution's limitations on legislative and even popular majorities are apparent not only from the Bill of Rights but also from the entire structure of government. Bicameralism and the separation of powers make it difficult for mere majorities to pass legislation. By dividing powers between the federal government and the states, the original Constitution further restrained the powers of a majority of the national legislature. We believe that a constitutional amendment requiring a supermajority to raise taxes is completely in accord with the overall objectives of the original Constitution, because a supermajority rule will both advance the interests of popular as opposed to legislative majorities and protect the individual rights of property and enterprise.

One of the fundamental problems of modern democratic politics is that concentrated interest groups have more influence with legislators than diffuse groups, even if the diffuse groups are a numerical majority.[3] Public choice theory suggests, and observations confirm, that political entrepreneurs will therefore tend to favor a legislative agenda that provides benefits to cohesive and organized interest groups while imposing costs on the electorate as a whole.[4] Our present budget crisis is in large measure a reflection of repeated instances of this dynamic. Legislators will trade votes to provide entitlements and other expenditure programs to numerous concentrated interest groups.[5] The taxes (or debt) required to pay for expenditures do not impose a very substantial constraint on such activity because the incidence of the taxes (or debt) can be diffused over the entire population (and future generations if possible). Thus, a constitutional rule that requires a supermajority to raise taxes can be understood as a rough attempt to restore a more rather than less democratic balance between those adversely affected by taxes and those advantaged by expenditures.[6] It functions as a precommitment by the society not to go down a road that will make everyone worse off in the end as concentrated interest groups demand expenditures that beggar the nation as a whole.[7]

Moreover, because taxes encroach on the right of each individual to enjoy the fruits of his labor, the amendment also attempts directly to facilitate the protection of liberty. The Framers themselves were intensely concerned to protect property rights of citizens. They believed that these rights were natural rights that inhere in each one of us and that respect for such rights would lead to economic growth and the progress of civilization. Therefore, the original Constitution provided substantial direct protection to property and enterprise through such provisions as the

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[1] *See, e.g.*, Akhil R. Amar, *The Bill of Rights as a Constitution*, 100 YALE L.J. 1131, 1147–52 (1991) (suggesting that the original purpose of the First Amendment was to permit popular majorities to bring pressure to bear on potentially unrepresentative national legislative majorities).

[2] *See* John O. McGinnis, *The Partial Republican*, 35 WM. & MARY L. REV. 1751, 1760 (1994) (outlining manner in which Constitution is designed to protect individual rights).

[3] MICHAEL T. HAYES, LOBBYISTS AND LEGISLATORS: A THEORY OF POLITICAL MARKETS 91 (suggesting that concentrated interests and costs are more likely to generate political and lobbying activity by organized groups).

[4] *See* E. Donald Elliott, *Constitutional Conventions and the Deficit*, 1985 DUKE L.J. 1077, 1090 (noting that government spending programs provide concentrated benefits while spreading the costs of programs over large and diffuse groups).

[5] The scenario is thus a specific example of the well-known paradox of vote trading. *See* William H. Riker & Steven J. Brams, *The Paradox of Vote Trading*, 67 AM. POL. SCI. REV. 1235, 1236 (1973) (stating that "[t]his paradox [of vote trading] has the property, that, while each trade is individually advantageous to the traders, the sum of the trades is disadvantageous to everybody, including the traders themselves.")

[6] It might be argued that the supermajority rule would actually give special interest greater power because special interests would need only two-fifths of a house to block legislation. The effects of supermajority rules on special interests will depend on the circumstances. While supermajority rules in some areas could give special interests even greater power, this is not true of a supermajority taxation rule. It has been our argument, which public choice theory supports, that special interests have generally exercised their power to secure benefits that have required increases in government spending and taxes. Because the supermajority taxation rule makes it more difficult for special interests to increase spending and taxes, it thus impedes the power of special interests.

[7] The Constitution is itself a societal precommitment to limit the range of future choices, because it is thought that choices prohibited by the Constitution will be generally socially disadvantageous. *See* Donald J. Boudreaux & A.C. Pritchard, *Rewriting the Constitution: An Economic Analysis of the Constitutional Amendment Process*, 62 FORDHAM L. REV. 111, 123 (1993).

Contracts Clause and the Takings Clause.[8] Moreover, it provided indirect protection by establishing structures that would make it more difficult for government to expropriate the people's wealth. For instance, federalism encouraged regulatory competition between different regimes thus restraining the power of factions: if the regimes became too oppressive or too inefficient individuals could always leave.[9] The separation of powers and bicameralism raised the costs to factions of getting control of the entire government.[10]

Unfortunately, the constitutional protections for the rights of individual enterprise have largely disappeared in the last fifty years. The protections for property have been substantially curtailed. With the demise of any restraints on Congress' power under the Commerce Clause, federalism has been gravely weakened.[11] With the rise of the administrative state, the separation of powers is a shadow of its former self.[12] Therefore there is a pressing need for structural amendments, like the supermajority taxation amendment, which would revive protections for the rights of individual enterprise. A society that constitutionally protects such rights is much more likely to enjoy long-term economic growth and prosperity.

Now let us turn to some specific concerns about the actual drafting of the amendment. First and most important, we believe that the amendment would be improved by provisions requiring a balanced budget. An amendment that restricts tax increases without limiting debt might increase debt as political entrepreneurs move to meet the demands of concentrated interest groups by increasing debt—subject to a simple majority rule—rather than increasing taxes. An even more effective method of limiting the power of concentrated interest groups would be simply to require a supermajority for all new spending programs, other than those strictly necessary for national security. Nevertheless, even in the absence of provisions requiring a balanced budget or subjecting spending provisions to a supermajority vote, a supermajority taxation amendment would be beneficial, because restrictions on tax increases function, especially in the long run, to limit wasteful spending on behalf of concentrated interest groups.

While it might be argued that any reduced taxes will merely be replaced with increased debt, this is not true. There are checks on Congress' ability to run large deficits; otherwise, Congress would lower taxes and run much larger deficits. Both taxes and debt are generally opposed by voters, but to different degrees and by different groups. Public choice theory suggests that if Congress is not otherwise constrained, it will finance spending with that combination of taxes and debt that minimizes the opposition to the program it passes. Any rule, such as a supermajority taxation amendment, that forces Congress to alter this combination should thereby increase the opposition to Congress' financing and spending program and therefore lead to less spending. In other words, if the amendment forces Congress to finance spending with larger deficits that are even more unpopular than higher taxes, this will induce Congress to spend less than it otherwise would have.

This theoretical argument is confirmed by political observation. Large deficits are now cited particularly by the new Republican majority as the primary reason to cut spending.[13] Indeed, both supporters and critics of the Reagan tax cuts of the early 1980s have respectively celebrated and deplored the curtailment of government expenditure that the resulting deficits appeared to cause.[14]

Second, we believe that Congress should carefully consider the role of the President in the legislative process resulting in tax increases. As the draft of H.J. Res. 49 stands, it is unclear what, if any, role the President has in the process. The Framers had strong reasons for giving the President a veto in the legislative process, including the process that leads to taxes increases: the President is uniquely

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[8] *See* Jonathan R. Macey, *Competing Economic Views of the Constitution*, 56 GEO. WASH. L. REV. 50, 57 (1987) (suggesting that the purpose of the Constitution was to guide transactions from public to private markets because private markets are better at creating wealth).

[9] Richard A. Epstein, *Exit Rights for Federalism*, 55 J. LAW & CONTEMP. PROB. 147, 149 (Autumn 1992) (arguing that federalism is a check on the monopoly of government power because individuals can leave.

[10] Macey, *supra* note 8, at 76.

[11] For a discussion of the collapse of federalism of powers, see Richard Epstein, *The Proper Scope of the Commerce Power*, 73 VA. L. REV. 1387 (1987).

[12] For a discussion of the collapse of the separation of powers, *see* Gary Lawson, *The Rise and Rise of the Administrative State* 107 HARV. L. REV. 1231 (1994).

[13] *See* Kenneth J. Cooper, *House Panel Softens Defense Measure*, WASH. POST, Feb. 1, 1995 at A–1 (noting that Republicans had to reduce their own planned defense expenditures because of pressure to reduce the deficit).

[14] *See* Daniel Patrick Moynihan, *Sick of Stockman and LaRouche*, THE NEW REPUBLIC, May 26, 1986 at 16 (observing that both Friederich Hayek and Moynihan believed that the deficits were "deliberately created to force a great reduction in the size and activities of the federal government: Hayek approved of the strategy while Moynihan did not).

the representative of the nation as a whole and his participation makes it harder for any single transient faction or coalition of factions to work their will in a moment of political passion. Moreover, his participation brings the opportunity for more deliberation. This is obviously true when he exercises a veto because then Congress must vote again to pass the legislation. But the mere potential of a veto forces Congress to take another powerful and sophisticated viewpoint into account throughout the process.[15]

Therefore we strongly recommend that the President be expressly provided with a veto in the process leading to tax increases. While we do not recommend a particular numerical supermajority for a supermajority tax amendment, it would be wise to require an even greater supermajority majority to pass a tax increase over a presidential veto. For instance, if the congressional supermajority stayed at two thirds, the veto override majority might be three quarters.

Finally, we note that term "tax" is undefined in S.J. Res. 49. We believe it would be prudent to have a definition. Without a definition crafted with the purposes of this amendment in mind, courts might construe the term tax as it is construed elsewhere in the Constitution to possibly unfortunate effect. Second, the political process will lead to pressure to attempt to characterize a tax as something other than a tax in order to avoid the supermajority requirement. A definition would serve as a barrier to these pressures. We would be pleased to work with your staff to shape an appropriate definition.

Senator BROWN. Mr. Strauss.

STATEMENT OF DAVID A. STRAUSS

Mr. STRAUSS. Mr. Chairman, thank you for asking me to appear before you. I have submitted a written statement for the record. In these remarks, I would just like to highlight four points, and I should say these points go not to questions of tax policy, which is not my academic subject, but rather to the wisdom and practicality of amending the Constitution to accomplish whatever tax objectives we want to accomplish. It seems to me, Mr. Chairman, these proposed amendments are an effort to provide really a quick fix to a complex problem and the Constitution is not the place for a quick fix.

First, it seems to me this amendment is really at odds with any serious effort to undertake tax reform. As we speak, Mr. Chairman, there are bleary-eyed tax lawyers at work poring over the Internal Revenue Code digging out loopholes for their clients for tax year 1996, loopholes that the Congress might not have expected when the laws were passed, loopholes that you only discover by spending many hours of well-financed work, work financed not by the middle-class people of whom Secretary Kemp spoke so eloquently, but by taxpayers who can afford these lawyer's fees.

Any loopholes they find once this amendment is in effect will, in effect, be frozen into law. They can be rooted out only by a two-thirds vote of both Houses, which means if there is any significant amount of support for the loophole, it stays in place.

I don't know of anyone who thinks that it is now too easy to adopt tax reform even to get rid of the most egregious loopholes or over-complexities. I don't know of anyone who thinks it is too easy. I think there is no question that this proposed constitutional amendment will make it much harder still.

My second point is that it seems to me this amendment is at odds with the objective of cutting the budget deficit, and here I think the point is a pretty simple, indeed mechanical one. If you

[15] For a discussion of the President's veto power, *see* Steven R. Calabresi, *Some Normative Arguments for the Unitary Executive*, 48 ARK. L. REV. 23 (1995); Michael B. Rappaport, *The President's Veto and the Constitution*, 87 NW. L. REV. 735 (1993).

pass an amendment that makes it more difficult to raise taxes without making it any more difficult to spend more, you will increase the budget deficit.

Senator Kyl pointed very effectively, I thought, to the unpopularity of raising taxes. Of course, raising taxes is unpopular. Spending more, however, is not unpopular and that is how we got into our current fix. If you make it even more difficult to raise taxes, it won't be any less popular to increase spending or maintain spending at the same level. That is a formula for an even greater budget deficit. The balanced budget amendment nearly passed the Senate about a year ago. I have a difficult time understanding how someone can be in favor of both this amendment and the balanced budget amendment.

My third point is actually one that I haven't seen featured in the debates over this amendment, but I think it is an important one, and it is that the effect of this amendment might very well be, yes, to lower the tax burden on American citizens, but greatly to increase the regulatory burden. There is more than one way to fund a government program. You can do it by raising taxes or you can do it by simply insisting that private individuals fund it themselves out of their own pockets. Then the money won't ever pass through the Treasury and it won't look like a tax increase.

If you want to fund government health care and you can't raise taxes, what do you do? Well, you insist that employers provide health care for their employees. That is not a tax increase and won't be subject to this amendment, but it will hit employers every bit as hard as a tax increase. If you want public housing and you can't raise taxes to pay for it, what do you do? You require developers to provide public housing as a condition of building their own housing. That will hit them just as hard as a tax increase, but it won't be subject to this amendment.

I think the passage of this amendment will simply create more circumvention of that kind. The Government will accomplish its objectives in a way that will be just as burdensome and potentially much more intrusive and much more wasteful than a straightforward, visible tax increase that people can debate. Then they can decide whether these Government programs are worth it or not. Secretary Kemp spoke about the need to avoid—I think his words were a circuitous and surreptitious means of funding Government programs. This simply puts a premium on finding surreptitious means of avoiding something that is nominally a tax increase.

My final point, Mr. Chairman, is to try to focus not, as my friend, Professor McGinnis, said, on the concept of a constitutional amendment, but on the fact that when you add an amendment to the Constitution, you are adding specific language, and in our system that means language the courts are going to interpret. If this provision becomes part of the Constitution, it will be the courts who will decide, if you tax Social Security benefits, is that an increase in taxes or is that just a reduction in entitlement spending.

If you increase charges for using Federal waterways, is that just a user fee and therefore not a tax or is that a tax? If you increase taxes in one respect but cut them in the other and they purport to be offsetting so as not to trigger the amendment, does that trigger the amendment or doesn't it? It will be the courts who will be de-

ciding these questions of fiscal policy, really, and deciding them over and over again.

In our system, if you add an amendment to the Constitution and the amendment's terms are controversial, as these terms will be, and adds some bite, as these certainly will, what that means is increasing the power of the courts, and the separation of powers implications of that, I think, are an important reason to hesitate and think long and hard before adopting amendments such as this.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Strauss follows:]

PREPARED STATEMENT OF DAVID A. STRAUSS

Mr. Chairman, thank you for the opportunity to appear before you to testify on S.J. Res. 49 and H.J. Res. 169. These proposed constitutional amendments would require supermajorities of Congress before legislation could be enacted to raise taxes. For a variety of reasons, both of these proposed amendments seem to me ill-advised.

S.J. RES. 49

Section 1 of S.J. Res. 49 provides that "[a]ny bill to levy a new tax or increase the rate or base of any tax may pass only by a two thirds majority of the whole number of each House of Congress." It would, in my view, be a serious mistake to adopt any constitutional amendment of this form, for a number of reasons:

- The amendment would be the death knell for tax reform.
- The amendment would be almost certain to lead to increased budget deficits.
- The amendment would be likely to bring about an increase in wasteful and inefficient regulation, as a substitute for taxation.
- The amendment, if it is to be more than symbolic, would undermine the separation of powers by effectively granting unaccustomed new powers to the courts.

I will address these points in turn.

1. *The amendment would be the death knell for tax reform.* Any serious effort to reform the Internal Revenue Code would, under this proposed amendment, require a two-thirds vote of each House and would therefore be extremely difficult to enact. This would not just be true of largescale, "structural" reform of the tax laws; it would also be nearly impossible to remove what most of us would consider to be loopholes.

Loopholes in the tax laws can arise because of well-organized lobbying efforts. They can also arise just because of inadvertence; in drafting something as complicated as the tax laws, it is impossible to foresee every contingency. And of course the tax bar is endlessly creative in trying to find loopholes that might benefit clients.

S.J. Res. 49, and any constitutional amendment like it, would apply to any legislation that closed a tax loophole. Eliminating a loophole, almost by definition, "increase[s] the rate or base of a tax." Any interest group that has obtained favorable treatment in the tax laws can, under S.J. Res. 49, rest easy. Groups that benefit from favorable tax treatment fight vigorously to maintain their advantage and often prevail even when only a majority vote is required to defeat them. If S.J. Res. 49 became part of the Constitution, such a group could be sure that, so long as it can obtain support from one-third of the members, plus one, of a single House of Congress, its loophole will remain intact. By the same token, every slip in the drafting of the tax laws will now become much more difficult to repair. If the slip creates a windfall for someone, the recipient of that unintended benefit will, under a provision like S.J. Res. 49, have a much easier time blocking any corrective legislation.

Larger-scale tax reform will also be, for all practical purposes, impossible. Virtually any reform of tax rates will require some increase in the tax base or in some individuals' tax rates, or both. This is conspicuously true, for example, of the much-mooted flat tax. As I understand it, the flat tax (and other tax simplification efforts) have as a centerpiece the elimination of some deductions. But eliminating deductions increases the tax base. And tax reform is also frequently concerned with rates. The flat tax in particular, unless it were to reduce revenue dramatically, will necessarily have to raise some tax rates while lowering others.

Dealing with unexpected loopholes ought to be part of the day-to-day business of administering the tax laws. It should not require an extraordinary, supermajority vote in both Houses of Congress. Beyond that, few people, I believe, would deny that

the tax laws could usefully be reformed in a broader way. And few would deny that tax reform is difficult to enact now. Indeed I know of no one who thinks that, even now, it is easy—much less *too* easy—to remove loopholes from the tax code. It is difficult to see any justification for amending the Constitution to make tax reform even more difficult.

2. *The amendment would be almost certain to lead to increased budget deficits.* S.J. Res. 49 creates high barriers to tax increases but no barriers to spending increases. It does not take much economic sophistication to see that the almost certain effect of doing this—making it much harder to tax but not much harder to spend—will be to increase the budget deficit.

Proponents of S.J. Res. 49 and similar proposals argue, I believe, that making tax increases all but impossible will effectively put pressure on Congress to limit spending increases too. That may be true. But it is hard to believe that Congress will limit spending increases to the same extent—in practical terms, nearly zero—to which S.J. Res. 49 limits tax increases. If a constitutional amendment is needed to keep Congress from raising taxes—keeping in mind that raising taxes is politically very unpopular—then surely one cannot expect Congress voluntarily, without any constraint comparable to a constitutional amendment, to impose similar limits on politically popular spending increases.

Opinions differ, of course, on what should be done about the budget deficit. But a proposed balanced budget amendment to the Constitution received the support of nearly two-thirds of the Senate. It seems to me nearly impossible to reconcile a belief in a balanced budget with support for an amendment, like S.J. Res. 49, that is virtually certain to precipitate greatly increased budget deficits.

3. *The amendment would be likely to bring about an increase in wasteful and inefficient regulation, as a substitute for taxation.* If tax increases become much more difficult to enact, we can expect legislators to find other ways to accomplish the objectives they would otherwise pursue by raising taxes. Suppose that the government wanted to fund a new program to supply (for example) health care or job training. Without a constitutional amendment like S.J. Res. 49, Congress might simply enact a tax increase to pay for those services. The cost of the program would be visible, and citizens could consider whether the potential gains were worth it.

A constitutional amendment like S.J. Res. 49 would not prevent the government from enacting, and funding, the same kind of program. How would the supermajority requirement be avoided? Simply by requiring private employers to furnish the services and to pay for them out of their own pockets. The effect on the private employers would be the same as the effect of a tax; the only difference is that instead of paying the money to the government, employers will be spending the money in the way the government directs. Such legislation, by the way, could not plausibly be treated as "raising taxes" within the meaning of S.J. Res. 49; if it were, then almost any regulatory requirement imposed on a private firm could be regarded as a tax increase subject to a supermajority requirement.

Sometimes employer mandates are better policy than a direct tax; sometimes they are not. But the decision between those options should be made on the basis of the relevant policy considerations. If it is dictated instead by the need to avoid a supermajority requirement, then the likely result will be economically unwarranted regulation and a wasteful distortion in the market in situations where an increase in taxes is the preferable course. The net effect on individuals of an amendment like S.J. Res. 49 could, therefore, easily be not less but more government-imposed burdens, and more inefficiency.

4. *The amendment, if it is to be more than symbolic, would undermine the separation of powers by effectively granting unaccustomed new powers to the courts.* It is often said that many nations have constitutions that are better than ours—on paper. Our Constitution is distinctive because it does not just exist on paper. It is enforced, generally by the courts. But this means that in considering amendments to the Constitution, it is not enough to decide that the amendment expresses a generally good idea. It is important to consider also how the amendment will be enforced in practice.

Any constitutional amendment that resembles S.J. Res. 49 would raise an enormous number of very difficult interpretive questions. And were a measure like S.J. Res. 49 added to the Constitution, it would not be long before the courts were asked to enforce it. Someone would claim that legislation enacted by a simple majority in fact "lev[ied] a new tax" or "increase[d] the rate or base of a□ tax" and was therefore unconstitutional. At this point the courts would have two choices. They could decide that Congress, not the courts, was to make the determination whether a bill required a supermajority vote. That approach would essentially make the new amendment symbolic—a statement of principle that Congress could evade at will.

Alternatively, the courts might decide to treat the new amendment as they treat most of the rest of the Constitution—to interpret and enforce its terms themselves. This would immediately require the courts to answer any number of difficult questions. Is a user fee—for example, a charge for the use of federally maintained waterways—a "tax" that requires a supermajority? Suppose all the proceeds from a certain exaction are paid into a trust fund, and the sums in that trust fund are used only for a specific purpose. Is that a "tax"?

Or suppose a law is adopted that increases taxes on some government benefits, such as social security. Is that a tax increase or just a reduction in the amount of the benefits? If the former, then why wouldn't any reduction in benefits count as a tax increase (thus effectively dooming any effort to reduce government spending)? If the latter, then couldn't Congress avoid the supermajority requirement just by describing an apparent tax increase as a reduction in the value of government benefits, since nearly everyone receives government benefits in some form?

Perhaps the courts could work out sensible and practicable answers to these questions. But the effects on the separation of powers would be profound. Judicial decisions would play a more central role in determining economic policy than they have ever before in our history. The fate of statute after statute would be uncertain until the courts had spoken. Legislation would have to be carefully tailored to the latest judicial pronouncements. There would be a premium on carefully structuring legislation—not to achieve the desired purposes in the most efficient way possible, but to work around the relevant Supreme Court precedents.

Alternatively the courts might decide that these difficult interpretive questions are for Congress to resolve; the courts might say that they will simply defer to Congress's declaration that a particular measure is or is not a tax increase. But then the new constitutional amendment would become, in essence, just an abstract statement of principle—something that Congress could effectively disregard whenever it chose to do so. One of the glories of our Constitution is that it is not filled with such abstract declarations of principle. It is, for the most part, an enforceable legal document. If we are to break with that tradition, we should be clear that we are doing so, and clear that it is worthwhile to do so.

H.J. RES. 169

Section 1 of H.J. Res. 169 provides as follows:

> Any bill, resolution, or other legislative measure changing the internal revenue laws shall require for final adoption in either House the concurrence of two-thirds the members present, unless that bill, resolution, or measure is determined at the time of adoption, in a reasonable manner prescribed by law, not to increase the internal revenue by more than a de minimis amount.

One difficulty with H.J. Res. 169 should be noted at the outset. H.J. Res. 169 refers only to "measure[s] changing the internal revenue laws." If the phrase "internal revenue laws" is taken to refer simply to Title 16 of the United States Code, then H.J. Res. 169 itself contains a loophole large enough to render the entire proposal almost useless. Congress can evade any requirements simply by raising funds through some other part of the U.S. Code. On the other hand, if that phase is interpreted more generally to mean "tax measures," then all the questions I mentioned earlier—what kind of measures count as tax laws?—return with a vengeance.

Even if this problem could be solved, however, H.J. Res. 169, or a measure like it, would, if taken at its word, have effects that no one—especially the most vigorous proponents of tax cuts—should endorse. One popular theory—sometimes called the "supply side" approach—holds that certain tax cuts stimulate economic activity and thereby increase revenues. There is, of course, great disagreement over how often tax cuts have this effect, and how great the effect is. But nearly everyone, I suspect, would agree that sometimes at least tax cuts can have that effect, and that at least if economic stimulus is desirable such tax cuts are useful.

But this kind of tax cut is exactly the sort of measure that would be difficult to enact under H.J. Res. 169, at least if the language of that provision is taken literally. That form of tax cut does "increase the internal revenue by more than a de minimis amount"—that is the putative attraction of such tax cuts. Therefore it appears that, if H.J. Res. 169 were to be added to the Constitution and implemented in the way its language suggests, one of the most popular and attractive form of tax cuts would be a thing of the past.

H.J. Res. 169 also presents many of the other difficulties that I mentioned in connection with S.J. Res. 49. While tax cuts that stimulate the economy and increase revenues would be barred, tax cuts that reduce revenues—and thereby increase the

budget deficit—would be encouraged. Also, like S.J. Res. 49, H.J. Res. 169 will encourage Congress to substitute regulation for taxation. Rather than receiving money from taxpayers and then spending it on a program, Congress could simply require the taxpayers to spend the money directly on the program. Individuals and firms could be required to clean up the environment, to build public housing, and so on. No money would pass through the treasury and the terms of H.J. Res. 169 would not be implicated. It is difficult to see why Congress should be encouraged to take steps in this direction, which will only conceal the costs of government programs and lead to market distortions.

Perhaps the most conspicuously problematic feature of H.J. Res. 169, however, is that as a constitutional amendment it seems to accomplish literally nothing. All of the difficult questions are postponed. H.J. Res. 169 envisions that Congress will enact legislation specifying how the "determin[ation]" that a measure has not "increase[d] the internal revenue" is to be made. The amendment itself does not explain how that determination is made.

But everything hinges on that determination. How are the economic effects of a change in the tax laws to be estimated? How far will those making that judgment go in trying to estimate the effects on behavior? How far into the future will the projections be made? H.J. Res. 169 provides no guidance at all on how these judgments are to be made. It in effect defers such judgments to a mechanism that is to be established by implementing legislation.

Since these judgments are made pursuant to legislation—rather than pursuant to the language of the amendment itself—the amendment itself, is an important sense, accomplishes nothing. Congress already has the power to enact statutes (or to adopt internal rules) requiring that legislation have certain revenue effects. Congress does not need H.J. Res. 169 or a similar constitutional amendment to empower itself to adopt such measures. Moreover, anything that is accomplished by legislation can be undone by legislation. A law increasing taxes need only contain a clause specifying that the implementing legislation, envisioned by H.J. Res. 169, does not apply to this particular tax increase. Congress might of course try to make the implementing legislation difficult to amend. But it can try to do that now.

S.J. Res. 49 and H.J. Res. 169 are powerful symbolic statements of antipathy to increased taxation. As symbolic statements they have much appeal. Few of us like taxes, especially on April 15. But these two resolutions are not offered just as symbolic statements—they are offered as amendments to the Constitution of the United States. As constitutional amendment they seem to me to be not as well conceived or as well thought through as they should be, and they should not be adopted.

Senator BROWN. Thank you.

Senator Kyl.

Senator KYL. Thank you. Both of you made excellent statements and let me begin by saying that, Professor McGinnis, I agree with what you said and I think you add significantly to the debate by framing it the way you did. Of course, Professor Strauss, I have some quarrel with what you said, but I also think you made some very valid points and I would like to explore those.

First of all, it will be harder and courts will have to answer some questions and there could be a move to require others to pay. I think all of those things are true and I think they are legitimate issues to raise. You also said you thought if the objective were one agreed to here that we could better achieve it by limiting spending. I also agree with that. That is why I am the sponsor of a constitutional amendment which would limit spending. I prefer that to a limitation on taxes, but failing the ability to get that passed, I have signed on to this proposition.

Let's go down through the list of things you talked about. No. 1, you said that this is a quick fix. I can assure you that amending the Constitution is never quick. As you point out, it is going to take two-thirds of both Houses—we won't get that passed this year—and then three-fourths of the States. This is going to take a long time. This is not a quick fix.

The quick fix when we have a deficit problem is to quick pass a tax increase, so this is designed to get away from quick fixes and to take a long, laborious time to get a constitutional amendment approved.

You said that it is not too easy today to make changes in the tax code. Well, there have been 4,000 changes just in the last 10 years—4,000 changes to the income tax code. As a matter of fact, the average that the tax code stays intact is 1.3 years, so it is very easy today to make changes in the tax code.

I think you are right that a lot of them deal with the special-interest benefits. Someone called them loopholes and used that term very broadly, and I think it covers a lot of what has occurred. I do agree with you that it would be harder to get rid of tax loopholes. That is one reason I think it would be preferable to have this amendment take effect after fundamental tax reform rather than before.

You also asked how one could be for this and the balanced budget amendment. I would say easy, since I am in favor of both. You should achieve a balanced budget under today's circumstances by reducing costs, not by raising taxes. Indeed, as Jack Kemp and Pete du Pont both testified, reducing tax rates is a surer way to increase revenues than raising tax rates.

Finally, and this is the one I would like to have you make a comment on, this could result in Congress requiring others to pay the bills—a very important point. I think that would raise profound constitutional issues. I want you to reflect on that for a minute, if you would, particularly in view of some of the more recent decisions coming down from the Supreme Court, and also with respect to the protection of property rights.

There is a point at which, is there not, that the Court would have to confront the question of whether Congress had the authority to, in effect, take from businesses or from families by mandating that they pay for something that heretofore has been a Government obligation? Would you reflect on that for a moment, and then I would ask Professor McGinnis to reflect on that as well?

Mr. STRAUSS. Well, I think that is right, Senator Kyl, that you would put the courts in the position of deciding is this really just a hidden tax increase or is it legitimate regulation, but that question will be an extremely difficult one and will put the courts in the position of confronting the following dilemma.

Either they can basically go along with what Congress has done, and if Congress calls it a tax increase, it is a tax increase. If Congress calls it something else, we won't gainsay Congress' judgment, which I think will actually be the reflex courts will have. That just leaves the door open for, as you put it really better than I did, requiring someone else to pay the bills.

Alternatively, the courts might actually get into the nitty-gritty and try to say is this regulation or is this taxation, and then what you are doing is turning over an enormous chunk of power to the courts. Suppose the courts say stop dumping pollutants into the neighboring stream. Is that making you pay for the cost of environmental protection when, in fact, the Government should be paying for that, or is that legitimate regulation? That question could be argued both ways and you can proceed from there. Paying the mini-

mum wage—is that making you pay what should be a wage subsidy funded through the Government or is that legitimate regulation?

You can go down through the list of regulatory policies, some of which some of us might like, some of which some of us might not like and, about each one of them, characterize them as a hidden tax increase. If you put the courts in the business of drawing that line, what you are really doing is opening the door for a whole new realm of judicial activism in the area, really, of overseeing governmental policy under the guise of enforcing this amendment.

As I say, I think is the less likely, although possible scenario. The more likely scenario is there will simply be a large door left open for, in Senator Kyl's terms, requiring someone else to pay the bill even in circumstances where that would really be a very wasteful, inefficient, and undemocratic way to structure policy because if the Government wants to pay for something, it should forthrightly raise the taxes and pay for it.

Senator KYL. Professor McGinnis.

Mr. MCGINNIS. Yes. Well, I can't entirely agree with that because I think this would still—regulation would still be the second best alternative from the point of view of a rational legislature because if they would have preferred regulation in the first place, they would have done that rather than taxation. So I think this will still likely reduce the—if you look at the sort of total level of regulation and taxation, would reduce it.

We should think of ways to have effective regulation, if that becomes a problem, through either regulatory reform measures or through even constitutional reform measures. I quite agree with you, Senator, that the best kind of measure at all would be some kind of constitutional amendment that would require a two-thirds majority for increases in spending, and I would include under that regulatory spending which is a different form of spending. In fact, you really have to consider regulation as a kind of on-budget item in itself. So that would be, I think, my response to that.

On the question of judicial activism, I think we have to be a little wary of simply taking the judiciary out of this. The problem with the judiciary in the past 20, 30 years has not, I think, been simply that it has been activist in the sense of making decisions protecting constitutional liberties. That is what we want the judiciary to do, and if one of the purposes of this amendment is to prevent regulation from coming in and being a form of taxation, we would like the judiciary to protect against that.

What we need to have, though, is to structure a kind of Constitution which the judiciary is likely to enforce well, and I think this might actually—a fiscal Constitution may likely be a Constitution which the judiciary may be more faithful to because I think we have had great success in some areas of sort of technical law where the judiciary seems occasionally to become activist, and to be incorrect is to be in some areas of constitutional rights where there is the applause of the crowd and I am not sure that this kind of tough fiscal law would be that area of law. So I might be a little more willing to trust the judiciary in this area.

Senator KYL. Thank you. Both of those are very informed answers. I do want to make one thing clear, and that is that this

issue underscores the rationale for a spending limit as the ultimate better way to deal with the issue than a tax limitation. I still believe a tax limitation, though imperfect, is appropriate under these circumstances because as Mr. Strauss pointed out, there are two ways that one can get around this if one really wants to.

One is to increase the public debt in order to spend more money. The other is to load the obligation on the private sector somehow. A spending limit, however, precludes that. My constitutional amendment limits spending to 19 percent of the gross national product, the historical level of revenue collected by the Federal Government for 40 years. Revenues have been at 19 percent. But spending escalated to almost 25 percent. It is now back down in the 22-percent range, as I recall, but the economy has always adjusted very quickly to allow the Federal Government to collect 19 percent of the gross national product, period, varying just a percentage or two. If you had a spending limit, then it wouldn't avail the Government to either raise taxes or go into debt or unload the costs on the private sector. It simply couldn't spend more money.

Mr. STRAUSS. Well, Senator, if I may, I think the loading on the private sector—you would still have to face the same problem. When I spend money to clean up the effluent coming from my plant, does that count against the Government spending ceiling, on the theory that I am doing the Government's work, or doesn't it?

Senator KYL. Depending upon how the Government foisted the obligation, it is possible. We get too many things now where, for example, the Forest Service says, I would love to do that environmental impact statement, but we don't have time; if you will pay for it, we will do it. We are getting too much of that going on right now, but I do see your point and again appreciate the testimony that both of you have given today.

Senator BROWN. Let me ask both of you to think about this in a little different framework. We have been through a dramatic shift in this Nation. As I referred to in my opening remarks, for almost our entire history, with the exception of 2 separate years prior to 1930, all levels of government combined never exceeded 10 percent of our GDP. Since 1930, they have never been below it. Currently, we are approaching 40 percent of our GDP spent by government. It is money taken away from people who earn it and spent by all levels of government. It is a shift of power, in effect.

Obviously, some think that it is not near enough, that you need to do more in redividing the wealth of the Nation and redistributing it. Some think you should do less, but it strikes me that the Kyl proposed constitutional amendment is a very direct effort to address this problem, or opportunity, I guess, depending on your point of view.

The real impact is one that says there is an upper limit as to how much government, in this case the Federal Government, is going to take away from the citizens and redistribute it. I would be interested in your reaction to that. Are we at a point where we have taken too much from people? When we democratically elect our Members of Congress and the President, is it necessary to have a constitutional limitation on how extensive, how large, how great Government will grow? What is the reaction of each of you in that regard?

Mr. STRAUSS. Well, Mr. Chairman, I think I have a couple of thoughts on that. I think if you look at—well, two thoughts, really. I think what most students of the political process will tell you is that this isn't a matter of a gigantic shift, of a gigantic leviathan, so to speak, taking things over. It is rather a problem of interest group politics; that there are powerful interest groups that want their share. Each share alone isn't enough to push the Government past the breaking point, but each one of these groups is irresistible and when you sum them all together and when you add them all up, then you have got a problem that we have. That is the nature of the problem, is concentrated interest group power. Then the question becomes how to handle that, and that is the intractable problem.

My second thought related to that is that if you look at the way our system has handled the great shift—this is a great shift that has happened in the last generation or two, but it is not the first great shift in our history. There was an enormous expansion of the power of the national Government under the aegis of Chief Justice Marshall in the first decades of the republic and then a swing back toward the States, and then, of course, an expansion of the nationwide economy in the year after the Civil War, and then the progressive era with its effects on the political system.

All of these changes, except for one, we have handled not through passing a constitutional amendment or a series of constitutional amendments, but rather evolutionarily through the political process gradually. Whatever you think about the current state of the Government, we came upon it originally.

The beginnings of the origins of the welfare state go back at least to the beginning of this century, possibly much earlier than that. The New Deal is given credit or blame for this, but the New Deal really was just kind of a bigger step in a series of steps that led to this system. The one exception to that is, of course, the eradication of slavery, and that is not an example we want to replicate, where we really did go through a national trauma to change something.

So I think my advice to those who think—and I am not one who thinks, but my advice to those who think that the Government has simply gotten too big would be, OK, start scaling it back the way it was built up; do it step by step. That is the way our constitutional tradition has handled things. That is the way mature constitutional traditions handle things. They don't have these sudden changes where one party leaves power and another party takes over and everything is up for grabs. They do things gradually.

This took several generations to buildup. It is going to take at least a generation or two to dismantle it. If you want to dismantle it, do it that way rather than going for the sudden, unpredictable, possibly counterproductive break.

Senator BROWN. To that point, isn't this more properly described as a limitation on further increasing the share of the GDP that goes to government? At least that is my sense of it. This is not an effort to cut it back. This is simply an effort to limit the levels of increase. I don't know if you see it that way.

Mr. STRAUSS. Well, in part, that depends on how the calculation is done. If this, for example, protects against indexing, then the in-

flation rate will have the effect of scaling back. But I am really addressing now—sort of more the concept of—do we need a constitutional amendment to change the direction of the Government.

My concern about this amendment is more that it is just, as phrased, not the right way to go about the task it assigns itself because of the questions I raised. I was really addressing in my answer to you, Mr. Chairman, more the question, are we at a point where we really need to do some fundamental constitutional reshaping. I don't think so, but if someone does, then my advice would be to reshape the way the Federalists reshaped, the way the Jacksonian States-righters reshaped, the way the progressives reshaped, and the way the advocates of the welfare state that you now criticize reshaped.

Senator BROWN. You know, there is a wonderful landmark case on interstate commerce that comes to mind as you describe "reshaping." It strikes me that we have changed the Constitution; but probably the way we have changed it is through changing the way we interpret it.

I think of that 1940 case because it was the ultimate, I thought, in creative legal reasoning where the farmer who had grown wheat on his own farm and fed it to his family and consumed that wheat on his own farm, was held to have been engaged in interstate commerce. I thought the case showed that the judges and the attorneys in that case has attended very creative law schools and had a remarkable ability to reason beyond the realm of reason.

Mr. MCGINNIS. I might just disagree a bit with my good friend, Professor Strauss, that we have had some important amendments in the Constitution that have changed the power of Government vis-a-vis the citizen. The income tax is a very important amendment in that respect, and so it has not only been a gradual change, but it has been a change through amendments as well, and so I don't think this would be a radical break with tradition in that sense.

Second, I think the two problems I described—the interest group dynamic of the power of concentrated interest groups really only can be broken through a change in the constitutive system. The difficulty is once you go down that road with interest groups having greater and greater power and having entitlements and being wedded to those entitlements, one does need a sharp break. One does need, to use the words of a law professor at Yale, a kind of constitutional moment to restructure the Government.

It is very interesting to note that often the times countries get their fastest growth is after some crisis, sometimes a very dramatic crisis, because they are able to reinvent their constitution in a way that will protect property rights and the rights of enterprise. There has been a good deal written on this and I think we don't want—I think what you are trying to do, Senator Kyl, with your proposals for your amendments and, in general, what the Contract With America is trying to do is to try to take Americans' inchoate dissatisfaction with Government and create a Constitution out of it because one realizes that it is only by doing that that one is going to break the power of these interest groups and create a new stage of the kind that we see when new governments come into being. It is not quite as radical as that, surely, but it needs to be a con-

stitutive moment precisely because of the interest group problem that I think both Professor Strauss and I agree is a serious impediment to real change in Government.

Senator BROWN. Thank you. I want to thank this panel. I am reminded that changes in Federal power have come about in significant ways through constitutional amendments. The income tax, obviously avoiding the admonitions and restrictions on taxes in the Constitution, was a dramatic shift in power. Direct election of Senators turned out to be much more significant than I think most of the people at the time thought. The Federal power over the States in the 14th amendment obviously had a huge impact here. So my guess is there is some precedent for this kind of change, albeit in the opposite direction.

I will thank this panel and ask the next one to come forward, and I would ask—also, I think Congressman John Shadegg is here, the other prime sponsor of the Barton-Shadegg bill. Congressman, if you are willing, I would like you to join this panel.

Congressman you are with a distinguished panel of tax experts, so I warn you, you may be in trouble with this panel, but having warned you, will you start us off?

PANEL CONSISTING OF HON. JOHN SHADEGG, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA; GROVER G. NORQUIST, PRESIDENT, AMERICANS FOR TAX REFORM, WASHINGTON, DC; ROBERT GREENSTEIN, EXECUTIVE DIRECTOR, CENTER ON BUDGET AND POLICY PRIORITIES, WASHINGTON, DC; AND WILLIAM A. NISKANEN, CHAIRMAN, CATO INSTITUTE, WASHINGTON, DC

STATEMENT OF JOHN B. SHADEGG

Mr. SHADEGG. I would be pleased to start off. I appreciate this opportunity to testify before the subcommittee. I do have a written statement which I will insert for the record.

Senator BROWN. Without objection, the entire statement will be included in the record.

Mr. SHADEGG. Let me just begin by stating, while I may have a panel of tax experts here, I think I have some degree of expertise in this particular arena. In 1992, my State, the State of Arizona, put into its constitution, with the support of 72 percent of the voting electorate, a constitutional two-thirds supermajority requirement. We did that following a long history of repeatedly raising our taxes and we faced all of the arguments that you are hearing today—those, and indeed more.

Let me simply say I am an unabashed supporter of this idea and I believe its time has come. We did this through an initiative process. We gathered signatures from people throughout Arizona, placed the matter on the ballot and, as I said, it received the support of 72 percent of those voting in that election.

There really is a very simple premise behind this, and you in your last questioning of the last witness commented about the degree of precedent there is. Eleven other States have supermajority requirements in their constitutions. I believe it will go on the ballot in 4 to 5 additional States this coming year. In those States that already have it, they represent one-third of all Americans, if you

add up the population in those States with supermajority requirements already in their constitutions.

The simple premise is simply that if we as a Congress and as a Nation make it somewhat harder to extract additional tax dollars from the people of the Nation, this Congress and this Federal Government will be forced to spend the money it has more judiciously. To date, this Congress has, and prior Congresses in the recent past have a rather miserable record of restraining Federal spending. Therefore, I believe it is time that we deal with that issue and that we deal with it by placing a restriction in the Constitution.

The premise is a straightforward one of fiscal responsibility. Should Congress be more responsible about spending the money it has, and if you believe it should, then this amendment will force Congress to make it harder to spend money because it is harder to raise taxes.

There are those who fret about placing this kind of a restriction in the Constitution. You have probably already heard today there are 10 other supermajority requirements in the Constitution, and it seems that those who make that argument lose a simple premise. The premise is that constitutions exist precisely for the purpose of restricting a legislation majority that runs amuck; that is, they exist for the precise purpose of protecting a minority.

Let me cite just one example. In the Omnibus Budget Reconciliation Act of 1990, a legislative majority of this Congress enacted legislation which destroyed the livelihoods of a small minority of Americans. I am referring to the so-called luxury tax. While some would argue and did argue when it was enacted that it would deal with a simple additional tax burden on the wealthiest of Americans who buy luxury items, the hard, cruel reality of that tax was that it destroyed the yacht and boat-building industry in this Nation, one in which we led the world.

Now, who paid the consequences? Did wealthy Americans who purchase yachts pay the consequences of that tax? They did not. They had the opportunity to buy the same goods, expensive yachts and other materials that were taxed, overseas from other nations. But the people whose jobs were destroyed by that unrestrained majority were the skilled and semi-skilled laborers in the carpentry fields, in the fiberglass fields, whose jobs were destroyed by the unrestrained will of a majority.

I suggest that this is indeed, as George Will has proposed, a reasonable restraint, and that in view of the Supreme Court's expansive construction of the Constitution's Commerce Clause which has given this Congress powers not envisioned by the Framers of the Constitution—and I might remind those who argue that this issue was debated when the Constitution was adopted that, in fact, we did not have an income tax until the sixteenth amendment—this is, in fact, a rather reasonable proposal which would restore many of the values that the Framers had in mind. Had they envisioned a Government with the expansive authority which this Government now has, I think they would have been before you supporting this premise and suggesting that a constitutional supermajority requirement is indeed a proper restraint and to be worried about as much as the popular press would have you believe.

Thank you very much.

Senator BROWN. Thank you, Congressman. You are welcome to join us up here, if you would like to, later on.

Mr. SHADEGG. I would be happy to remain and answer questions if you have them.

[The prepared statement of Mr. Shadegg follows:]

PREPARED STATEMENT OF REPRESENTATIVE JOHN B. SHADEGG

Mr. Chairman, as one of the four chief sponsors of the Tax Limitation Amendment (H.J. Res. 159) in the House, I want to thank you and the members of the Subcommittee for holding this important hearing on Tax Day—the same day the House will vote on H.J. Res. 159. I would also like to thank you for the honor to appear before you today.

John Randolph, who served as a Member of this House and as a Member of the Senate between 1773 and 1833, contemplating the power of government once observed:

> "It has been said that one of the most delicious of privileges is that of spending other peoples' money."

Regrettably this privilege has been abused.

In 1992, I chaired Proposition 108, a state-wide initiative in Arizona, which was adopted by a vote of 72%, imposing a constitutional two-thirds requirement for further tax increases. Arizona is one of eleven states which has enacted a two-thirds supermajority approval of a tax increase. Let me briefly explain why I fought for the Arizona initiative.

Former United States Supreme Court Chief Justice Johnathon Marshall once wrote: "The power to tax is the power to destroy." He wrote those words before the Civil War at a time when the role of government was radically different than it is today. Given the size of government today, Justice Marshall's words ring true now more than ever.

The government's power to tax has become, quite literally, the power to destroy. The credit which is essential for American businesses has all but dried up as the government commands seventy-five percent of available credit to finance its spendthrift ways. Small businesses all across America—the lifeblood of our economy—have gone bankrupt in record numbers under the weight of excessive government taxation.

S.J. Res. 49, requiring a two-thirds majority to approve tax increases, is a reasonable and necessary reform. Given the radical change which has occurred in the role of government, it will provide discipline against the ever-increasing pressure to tax and spend.

Since 1981, the House has passed five tax increases. Four out of the last five major tax increases—totaling $666 billion—failed to obtain the support of sixty percent in both Houses. Under a supermajority, the 1993 Clinton tax increases—the largest in American history—would not have passed.

I was sent to Congress by the fourth congressional district of Arizona to balance the federal budget by shrinking the size and scope of government, not raising taxes. I have watched Congress go down this same road before. Each time Congress has promised to cut spending, what has happened instead is that taxes have increased. The chronic budget deficit is because Congress spends too much, not because it taxes too little.

The effects Arizona's Tax Limitation Amendment cannot be overstated. Prior to passage of Proposition 108 Arizona had raised taxes for eight out of nine successive years. Since passage of this Tax Limitation Amendment, taxes have not been raised and our economy, which had grown sluggish under a series of tax increases, is now booming.

Mr. Chairman, Arizona's example is proof that the Tax Limitation Amendment works while it protects taxpayers.

Senator BROWN. Grover Norquist, Americans for Tax Reform.

STATEMENT OF GROVER G. NORQUIST

Mr. NORQUIST. Thank you. I also have a prepared statement with some exhibits I would like to share.

Senator BROWN. They will be in the record.

Mr. NORQUIST. This a rather simple constitutional amendment to require a two-thirds supermajority to raise taxes, and those people

commenting on it fall into one of two categories, those people who think it would be a good idea to make it more difficult for Washington to raise taxes and reach into the pockets of the American people and those who think it would be a bad idea for it to be more difficult.

As a result, a lot of the discussion sort of obfuscates this distinction, but I think the American people understand perfectly well that we are going to go in one direction or the other. It will become more difficult to raise taxes or it will continue to be easy to raise taxes.

I would suggest that in listening to this debate today, tomorrow, and over the next several years, as this amendment will not pass next week or next month, but all constitutional amendments take time, listen to when people talk about, well, what about an emergency? Oddly enough, the opponents of this amendment always think of Washington's needs, Washington's emergencies, the Government's budget.

When they talk about your tax dollars, are they talking about money that you pay or are they thinking of it as revenue and inflow? So the division in politics on this amendment is very clear-cut. Some people want bigger and more Government and they are opposed to it. Those of us who want the Government not to grow and, in fact, hopefully to reduce in size as a percentage of the economy will support it.

Second, this is an amendment that comes from the States, just as the balanced budget amendment in the constitution in 49 States has finally begun to come to Washington. The House has passed it. The Senate is two votes and one election away from passing a balanced budget amendment. The line item veto in law in 43 States has also finally come, at least in part, to Washington.

Now, 10 States with supermajority requirements also speak to Washington to point out that California did not fall off the edge of the earth, that all of the objections that have been raised to this constitutional amendment might have been raised to California's or other States' and none of the dire consequences—judicial fiat, underfunding of State budgets or whatever—have taken place.

A third thought, and that is that those people who raise the question of national defense as a problem—national defense is less than a third of the Federal budget. If there were national defense needs, it is possible to reduce other spending if there really is an emergency. Of course, if there really is an emergency, it would be easy to get a two-thirds vote. Oddly, those people who raise national defense were opposed to spending money on national defense back when the Soviet Union existed, so I don't know how serious that concern is when raised.

Fourth, tax reform is coming. I believe, as some of the previous panelists have talked about, that we will be moving toward a flat tax, perhaps even toward a consumption tax. But if we end up with a President who is in favor of taxpayers over the next 4 to 5 years, we are going to have tax reform passed in the next 2 years that will look at a broader base, a flatter rate, and maybe even moving toward a national sales tax. This amendment is not going to get in the way of those reforms.

In fact, Americans for Tax Reform has commissioned a poll which shows strong support for the idea of a supermajority—over 70-percent support for a supermajority to raise taxes, regardless of how you ask the question, but 68 percent point out that they would be more likely to support fundamental tax reform, going to a flat tax, if they knew that this constitutional amendment protected them against having rates increase.

If we are going to take the rates down to 17, but Washington can start taking that up to 18, 19, and 20, that reduces people's interest in fundamental tax reform. So as somebody who supports moving toward a Forbes or an Armey flat tax, I think this amendment is necessary and needs to be moving before we look at such a project.

Last, for those comments that, gee, how could we do all the little changes that we do every year if you required two-thirds, the answer to that is you won't be able to. One of the goals of this amendment is to get some stability, and I know it will make it more difficult for some people to raise money if they can't threaten or promise tax hikes or tax reductions every few months, but I think that this measure will do more to reform campaign finances than any of the campaign finance reforms that are being put forward.

So at Americans for Tax Reform, we are strongly supportive of this amendment and we look forward to working every April 15 with the House and Senate until it passes.

Senator BROWN. Thank you.

[The prepared statement of Mr. Norquist follows:]

PREPARED STATEMENT OF GROVER G. NORQUIST

Thank you for inviting me to testify before your committee this morning on the important issue of a constitutional amendment requiring a two-thirds vote of both houses of Congress for any new taxes or increases in existing taxes. Americans for Tax Reform has been actively involved with state taxpayer groups around the country which are attempting to secure similar amendments in state constitutions, introducing similar legislation to state legislatures, and placing voter initiatives for constitutional tax limitation on state ballots. Introducing the concept of constitutional tax limitation at the federal level is a positive development in protecting American taxpayers from an ever increasing tax burden. I welcome this effort and applaud those Senators who have proposed constitutional tax limitation at the federal level, in particular Senator Jon Kyl (R–AZ), for their leadership in this debate.

Today, I wish to make the following five points in support of the Tax Limitation Amendment:

- Requiring a two-thirds majority of Congress for all tax increases is the best method for limiting the tax burden on United States taxpayers.
- Without constitutional tax limitation, it will be easier to raise taxes than to cut spending.
- Tax limitation promotes economic growth.
- Tax limitation is good government policy.

I. REQUIRING A TWO THIRDS MAJORITY OF CONGRESS FOR ALL TAX INCREASES IS THE BEST METHOD FOR LIMITING TAX INCREASES

Under the current rules, previous Congresses have been incapable of restraining their taxing and spending. The empirical evidence is compelling. The United States runs a chronic budget deficit because Congress spends too much, not because it taxes too little. During the post-war era, while total government revenues as a share of Gross Domestic Product deviated little from approximately 19 percent, spending has risen continuously, averaging 18 percent in the 1950s, 19 percent in the 1960s, 21 percent in the 1970s, to a range of 22% to 25% over the last ten years.

Congress has historically managed to avoid spending cuts and enact tax increases by some maneuver to provide political cover. For instance, in both 1990 and 1993 Congress voted to raise taxes in the guise of omnibus budget laws that were de-

scribed as deficit reduction acts. In the 1970s the government grew rapidly as inflation pushed workers into higher tax brackets and Congress did little to interfere.

Because Congress is unable to make small spending cuts it is forced to raise revenue by enacting targeted tax increases. Often, these piecemeal tax increases are the most damaging. Examples are numerous of their damaging effects. The eroding value of the dependent child exemption hurt families. Increases in the capital gains tax and lengthening of the depreciation of structures in the Tax Reform Act of 1986 destroyed real estate values and substantially contributed to the severity of the savings and loan collapse in the late 1980s. The luxury tax implemented under the Omnibus Budget Reconciliation Act of 1990 destroyed the yacht building industry in the U.S.

A. Two-Thirds is superior to other percentages

Requiring an affirmative vote of two-thirds of all Members of Congress is superior to other proportions.

1. Two-Thirds is the Percentage Used Throughout the Constitution

A requirement of two-thirds is consistent with constitutional supermajority voting requirements. In ten instances the Constitution mandates supermajority voting requirements. Each of these requirements reflects the thoughtful deliberation by the Framers and Amenders of the Constitution. Each serves a purpose and each illustrates the capacity of the Constitution's architects to impose such requirements on Congress where they were deemed necessary or useful. When it was appropriate in the political environment of the 1780s to prescribe a specific numerical voting requirement, the Constitution supplied one. The Constitution is a living document, adaptable to modern problems. It is clear that if the Framers of the Constitution had been faced with runaway deficits and massive government in the absence of a compelling national emergency, they would have required a supermajority for tax increases. In the present environment of high taxes and the need for either sharp cuts in government spending or increases in revenue, politicians in Washington, DC, cannot be trusted to protect the pocketbooks of Americans without a requirement that there be broad support for any tax increase.

2. Many States Mandate A Supermajority Vote of at Least Two Thirds For an Increase in Taxes

States around the country have been forced to reform their budgeting and tax policies due to their own deficit spending. Many states have been successful in trimming their deficits without raising taxes. The method used by the most successful states has been supermajority tax limitation laws and spending limitation laws. One third of all Americans live in a state with supermajority constitutional tax limitation. In most of the states with supermajority requirements the idea of requiring a greater than fifty percent vote of the legislature to increase taxes grew out of the tax revolt movement and the initiative process. These states offer a successful model for the Federal Government's budget and tax reform efforts.

- Two-thirds is the percentage used in most of the states requiring supermajority approval of tax increases.
- Two-thirds is the percentage used in most of the supermajority initiatives now working their way through the states for the November 1996 and 1998 ballots.
- Twenty-one states in 1995 and 1996 introduced legislation that proposed supermajority requirements for tax increases.

3. Two-Thirds is a Higher Standard

Two-thirds is a much higher standard which affords superior protection. It would require 290 votes in the House and 67 in the Senate. Four of the last five tax increases were passed with less than a two-thirds supermajority. These new taxes added $666 billion to the tax bill of the American taxpayer. Consequently, any tax measure that musters the required two-thirds vote will obviously enjoy wide-support from all political parties, and among the people generally.

II. WITHOUT SUPER-MAJORITY TAX LIMITATION POLITICIANS ARE BIASED IN FAVOR OF TAX INCREASES

Presidents for years have stated that one of their preeminent goals was to balance the federal budget. Unfortunately, this noble sentiment ran into one Congress after another that was addicted to deficit spending in order to appease their constituencies and effectively buy their way to re-election. Most responsible politicians now agree that the U.S. must balance its budget. However, there are countless plans for doing so. Many plans put forward by those "formerly" addicted to deficit spending propose increased federal revenues. In their view, the simplest way to increase fed-

eral revenues is to increase taxes. Whether it is an upward revision of the brackets, user fees, elimination of deductions or increased "investments," the bottom line is that many in Congress believe they cannot balance the federal budget without resorting to tax increases. In fact, while a member of Congress in 1992, White House Chief of Staff Leon Panetta testified in favor of a balanced budget act which mandated automatic tax increases!

There is no correlation between increased taxes and lower deficits. The fiscal history of the U.S. illustrates this point. In fact, data suggests that an increase in taxes of $1.00 actually leads to $1.59 of new spending. Throughout the history of the U.S. the tendency of Congress to spend additional taxes instead of using them to reduce deficits has continually increased. In the first decades of the nation, tax increases were associated with declines in the federal deficit. In the Twentieth Century, increases in taxes have resulted in higher deficits. Much of this increase in deficits and tax increases can be associated with the political advantages associated with new spending.

When politicians allocate government resources, they seek the highest political return. There is a bias in favor of tax increases to pay for government-delivered benefits that go to relatively few people. These people come together as special interests to effectively lobby Congress. Taxes, on the other hand, are spread among many millions of people across the country who find it very difficult to band together as an effective interest group. Without constitutional tax limitation, methods such as Leon Panetta's automatic tax increases would likely gain widespread support from special interest groups.

Many politicians opposed to the Tax Limitation Amendment maintain that the solution to runaway spending is not to amend the Constitution, but to simply enact balanced budget legislation. This is impractical. Using this approach to deficit reduction many of these same lawmakers voted for record tax increases in 1990 and 1993, effectively eliminating any tax relief enjoyed in the 1986 tax reform legislation. The result: the deficit, which was $152 billion and falling when President Ronald Reagan left office in 1989, is now almost $200 billion and projected to rise every year into the foreseeable future.

With a balanced budget law or amendment without a supermajority requirement there will be a bias towards increasing taxes as a means of complying with the law. Raising taxes presently only requires a simple majority vote. Weak amendments which require a supermajority to run a deficit, but only a simple majority to raise taxes make it easier to raise tax rates than to borrow. In effect they create a tax trap. If you require a supermajority vote for borrowing money and increasing the debt ceiling you must require the same mechanism for increasing taxes. You can hear the politicians now saying how they didn't want to do it, but the Constitution made them raise your taxes. Instead of reflexively raising taxes to comply with the law, Congress should be compelled to reduce spending as a means of balancing the budget.

III. TAX LIMITATION PROMOTES GROWTH

Available data show that the concept of requiring supermajority vote helps in the battle to lower taxes. Ten states presently have some form of supermajority requirement for tax increases. Eight of those ten states require a supermajority of at least two-thirds. In those ten states, taxes as a proportion of personal income have actually declined two percent. In states without a supermajority requirement taxes as a proportion of personal income have risen two percent. Thus, there is a difference of four percent in tax burdens in those states with supermajority tax limitation requirements. What has happened in supermajority states is that lawmakers are required to reach broad consensus before enacting tax increases. The supermajority forces state lawmakers to seriously consider spending priorities and makes them more accountable to their taxpaying constituents.

Not only do supermajority requirements lead to lower tax burdens at the state level, they have resulted in a reduction in overall state government spending. In states that require supermajority approval of tax increases, spending has increased by two percent versus an increase of nine percent in states without the requirement. A differential of seven percent equals significant reductions in government spending and taxation. A seven percent reduction in federal spending would go a long way toward balancing the federal budget.

IV. TAX LIMITATION IS GOOD GOVERNMENT POLICY

For over fifty years, concentrated and vocal interest groups have been able to secure costly benefits for themselves that are paid for by the widely-scattered majority of taxpayers. Due to its far-flung nature, the taxpaying majority is legislatively inef-

fective in stopping the grants of federal government largess. A Constitutional amendment mandating a two-thirds affirmative vote of Congress to increase taxes or eliminate deductions will improve the legislative process by making the passage of these expensive benefits harder to support. Requiring an affirmative Congressional vote for the increase of the tax burden will provide a "bright-line" test that all federal legislators must take before they can raise the tax burden of the U.S. people. When specialized interest groups seek a government benefit they will have to persuade a much larger group of legislators to support their handout. Legislators who represent the taxpayers who will pay the bill will have an easier time defending their positions and stopping the continued excess taxation of the American people. No longer will they be able to go home to their states and districts and say that they were compelled to raise taxes because the increase was attached to some monumentally important bill which required passage. Nor will they be able to claim that the Constitution mandated a tax increase. The excuse that "my hands were tied" will no longer be acceptable. All members of Congress will have to live, govern, and run for reelection on their voting record regarding tax increases, voting records for all to see and to compare.

Appendix A

Supermajority Requirements in the U.S. Constitution

Article	Applies To:
Article I, section 3, clause 6	Conviction in impeachment trials
Article I, section 5, clause 2	Expulsion of a Member of Congress
Article I, section 7, clause 2	Override a presidential veto
Article II, section 1, clause 3	Quorum of two-thirds of the states to elect the President
Article II, section 2, clause 2	Consent to a treaty
Article V	Proposing constitutional amendments
Article VII	State ratification of the original Constitution
Amendment XII	Quorum of two-thirds of the states to elect the President and the Vice President.
Amendment XIV	To remove disability of those who have engaged in insurrection
Amendment XXV section 4	Presidential disability

Appendix B

Supermajority Requirements at the State Level

State	Requirement	Year Enacted	Applies To
Arizona	2/3 elected	1992	All taxes
Arkansas	3/4 elected	1934	All taxes since 1934 except sales tax.
California	2/3 elected	1978	Property taxes
Colorado	3/4 elected	1992	All taxes
Delaware	3/5 elected	1980	Revenue increases
Florida	3/5 elected	1971	Changes in the corporate income tax rate
Louisiana	2/3 elected	1953	All taxes
Mississippi	3/5 elected		All taxes
Oklahoma	3/4 elected	1992	All taxes
South Dakota	2/3 elected	1978	For increased tax base and existing tax rates

Appendix C
State Supermajority Initiatives

State	Requirement	Applies To
Arizona	2/3 of those voting in an election	Existing state taxes or fees or creation of any new state taxes or fees that arise from the initiative process
California	2/3	All taxes
Florida	2/3	Voter approval of new taxes and fees
Maine	2/3	Legislative and/or voter approval of changes in state tax laws.
Michigan	2/3	Voter approval of tax increases and legislative pay raises
Nevada	2/3	All taxes
New York	2/3	All taxes over $50 million
Ohio	2/3	All taxes
Oregon	Supermajority	All revenue bills

Appendix D

Supermajority Legislation Introduced at the State Level in 1995 and 1996

State	Requirement
Florida	Constitutional amendment requiring two-thirds of both houses of the legislature to raise taxes.
Georgia	Constitutional amendment requiring approval of two-thirds of both houses of the legislature for increasing any tax, fee, assessment or charge imposed by the state.
Hawaii	Proposed amendment to the state constitution to require approval of two-thirds of both houses of the legislature to increase taxes or to repeal a tax exemption or credit.
Illinois	Requires three-fifths approval of both houses of the legislature for the imposition of new taxes, license fees or an increase of the effective rate of taxation.
Idaho	Supermajority of both houses of the legislature for any bill intended to generate revenue for the state or any political subdivision.
Indiana	Approval by the voters of new taxes or increases in existing taxes.
Maryland	Supermajority for any increase in income or sales taxes or any broadening of the income or sales tax base.
Massachusetts	Constitutional amendment restricting an increase in taxes without supermajority approval.
Minnesota	Two-thirds supermajority of both houses of the legislature, or approval by a majority of voters actually voting on the question, to create new taxes or increase the rate of existing taxes.
Michigan	Supermajority in each legislative chamber to approve an increase in income, sales, use, and single business taxes.
New Mexico	Three-fifths vote of the members of each house of the legislature present for new taxes or fees or increases in the rate or base of existing taxes or fees.
New York	There are seven bills pending that require a two-third

	supermajority approval of both houses of the legislature to increase taxes.
North Carolina	Requires a 2/3 vote of each house of the legislature to levy or increase taxes.
Ohio	Increases in State taxes must be approved by a supermajority of each house of the General Assembly.
Rhode Island	Supermajority required to increase sales, use or income tax.
South Carolina	Two-thirds supermajority required for property tax increases and retroactive taxes.
West Virginia	Requires a 2/3 vote for all bills imposing a tax or license fee, or increasing the effective rate of tax.
Wisconsin	2/3 supermajority in both houses of the legislature to create, expand, or raise taxes.

[1] See W. Kurt Hauser, *The Tax and Spend Equation*, Wall. St. J., March 25, 1993.

[2] Not surprisingly, these higher taxes were not used to trim the deficit. Instead, they fueled increased government spending. See Richard Vedder, Lowell Gallaway, and Christopher Frenze, *Taxes and Deficits: New Evidence*, Joint Economic Committee Study, 1991; Gerald W. Scully, *What is the Optimal Size of Government in the United States*, National Center for Policy Analysis, 1994.

[3] Due to the luxury tax on yachts, 9,400 Americans lost their jobs. The effect of luxury taxes when the cost to the Federal Government of increased unemployment is taken into account is to spend $2.40 for every $1 raised. For the yacht tax the direct cost to the government for each dollar raised was $3. *Deals, Deficits and Dynamic Forecasts*, Republican Views of the 1992 Joint Economic Annual Report, April 1992, p.7.

[4] See appendix A for a list of constitutional supermajority requirements.

[5] In fiscal year 1986 the states had an aggregate surplus of $60 billion, while the federal government had a deficit of $221 billion. See W. Mark Crain and James C. Miller III, *Budget Process and Spending Growth*, 31 Wm. & Mary L. Rev. 1021 (1990).

[6] Only in Delaware was the measure sent to the voters by the legislature. See, *Tax Limitation Amendment: Hearings on H.J. Res. 159 Before the Subcomm. On the Constitution of the House Comm. On the Judiciary*, 104th Cong., 2nd Sess. (1996) (statement of J. Kenneth Blackwell, Ohio State Treasurer).

[7] See infra. appendix B for a full list of present state supermajority requirements.

[8] See infra. appendix C for a full list of present state supermajority initiatives.

[9] See infra. appendix D for a full list of recent state supermajority legislation.

[10] See Tax Equity and Fiscal Responsibility Act of 1982 (House vote 226-207, Senate 52-47, $214 billion in new and higher taxes); Omnibus Budget Reconciliation Act of 1987 (House 237-181, Senate 61-28, $40 billion in new and higher taxes); Omnibus Reconciliation Act of 1990 (House 228-200, Senate 54-45, $137 billion in new and higher taxes); Omnibus Budget Reconciliation Act of 1993 (House 218-216, Senate 51-49, ($275 billion in new and higher taxes).

[11] The 1993 tax increase was the largest in U.S. history during peacetime. It did not even achieve the support of a majority of elected Senators. It only passed when vice-president Al Gore cast a tie-breaking vote in the Senate.

[12] David E. Rosenbaum, *The 1992 Campaign: Candidates on the Issues; Where They Stand on the Deficit*, N.Y. Times, October 5, 1992, at A17; Paul Blustein, *Nominees' Economic Goals Seen as Lacking Realism*, Wash. Post, October 20, 1988, at A1; *Carter Embraces Austerity - - For Now*, Econ., July 26, 1980, p.19.

[13] *Balanced Budget: Hearings on H.R. 5676 Before the Subcomm. on the Legislative Process of the House Comm. on* Rules, 102nd Cong., 2nd Sess. (1992) (Testimony of Leon E. Panetta, Chairman, Committee on the Budget).

[14] Richard Vedder, Lowell Gallaway, and Christopher Frenze, *Taxes and Deficits: New Evidence*, Joint Economic Committee Study, 1991.

[15] Id.

[16] Gerald W. Scully, *What is the Optimal Size of Government in the United States*, National Center for Policy Analysis, (1994), p.5. See, Jonathan R. Macey, *Public Choice: The Theory of the Firm and the Theory of Market Exchange*, 74 Cornell L. Rev. 43, 51 (1988).

[17] One needs to look no farther than the few thousand subsidized peanut farmers who easily overpower the millions of taxpayers who would do away with their subsidy. For an illustration of this phenomenon See Guy Gugliotta, *House, 270-155, Passes $46 Billion Farm Bill*, Wash. Post., March 1, 1996, at A6; Eric Schmitt, *House Vote Keeps Peanut and Sugar Price Supports*, N.Y. Times, February 29, 1996, at A19. The peanut subsidy survived by a vote of 212-209 in the House of Representatives.

[18] The Omnibus Budget Reconciliation Act of 1990 raised taxes by $137 billion. The Omnibus Budget Reconciliation Act of 1993 raised taxes by $275 billion and was the largest tax increase in world history.

[19] Daniel J. Mitchell, *Why a Balanced Budget Amendment Must Include True Tax Limitation*, Heritage Foundation, Backgrounder No. 237, Jan. 24, 1995, Update to Heritage Foundation Backgrounder No. 899, June 4, 1992.

[20] Such a scenario was a very real possibility under the Schaefer-Stenholm Balanced Budget Act of 1995 which required a supermajority to run a deficit but only a simple majority to raise taxes. Representative Stenholm claimed that his balanced budget amendment included tax limitation by requiring a majority of the whole membership, as opposed to a majority of those actually voting, to approve tax hikes. This would offer little protection to the taxpayer. Of the nearly fifty tax increases since 1962 only three failed to reach the supposed supermajority threshold of the Schaefer-Stenholm Amendment. Even those three increases, the Interest Equalization Tax Act of 1964, The Investment Credit Suspension Act of 1966, and The Surface Transportation Assistance Act of 1982 passed by lopsided margins of 45-28 in the Senate, 161-76 in the House, and 180-87 in the House respectively.

[21] See infra appendix B.

[22] Arkansas, Colorado and Oklahoma require a three-fourths percentage. See infra. appendix B for a chart on the percentages required by each state.

[23] Daniel J. Mitchell, *The McCain/Saxton Proposal: A Supermajority Antidote to Washington's Pro-Tax Virus*, Heritage Foundation, June, 1991. States with supermajorities saw their per capita tax collections jump by 87.35%. States without supermajorities saw their per capita tax collections rise by 104.41%. This translates to an increase that is 20% faster in states without a supermajority. Id. See, "State Revenue and Expenditure Report" (Washington D.C.: American Legislative Exchange Council, July 1990). See also, Joe Barton, *The Balanced Budget Amendment: Ending the Federal Spending Binge*, Remarks of Congressman Joe Barton, (R-TX) to the Heritage Foundation, January 5, 1995.

[24] See, *Tax Limitation Amendment: Hearings on H.J. Res. 159 Before the Subcomm. On the Constitution of the House Comm. On the Judiciary*, 104th Cong., 2nd Sess. (1996) (statement of J. Kenneth Blackwell, Ohio State Treasurer).

[25] The seven year balanced budget plan put forward in Congress by the Republicans in 1995 would have resulted in a balanced budget by the year 2002 by reducing the growth of government spending by 6-7%.

[26] This will put a stop to the practice of "logrolling" or the floating coalition where interest groups combine to pass packages of spending provisions that would never pass individually on their own merits.

Senator BROWN. Mr. Greenstein, Center for Budget and Policy Priorities.

STATEMENT OF ROBERT GREENSTEIN

Mr. GREENSTEIN. Thank you very much, Mr. Chairman. I think I am the lonely member of this panel who thinks that this is not a wise idea, and I view a lot of this in the context of some of the issues that came up before the Kerrey-Danforth Entitlement Commission in 1994, on which I had the privilege of serving.

As you may know, the commission forecast that under current tax and entitlement laws, the deficit would exceed 15 percent of the gross domestic product by the year 2030 if policies aren't changed. Many experts believe that to deal with this, we are going to need very strong measures that include combinations of both spending cuts and some revenue increases in the decades ahead.

One of my principal concerns is I believe this amendment would make it extremely difficult, if not impossible, to put packages of that kind together because of the two-thirds barrier. I am also concerned it would make it harder to put together balanced packages to address the serious financing problems in Social Security and Medicare that we face in the years ahead and that a two-thirds requirement would make it more difficult to deal in a deficit reduction context with some of the special interest tax expenditures which I think ought to be considered along with spending that is not needed or beyond what we can afford.

I note that even President Clinton's new budget, to go back into the details, forecasts a deficit equaling 12 percent of GDP in 2030 and about 25 percent of GDP by 2050. This means that deficit reduction measures far beyond those that Congress and the Administration are fighting over now are ultimately going to be needed, and I am very concerned in that context to have the two-thirds barrier.

When we were at the Entitlement Commission, one of the most interesting pieces of testimony we got was from Bob Reischauer, then the Director of CBO, and Reischauer said that when you look at this long-term fiscal forecast, what you would have to do to get all of the needed deficit reduction either just from programs or just from revenues—either scenario would very likely be unacceptable to the American public.

If you have to get all of it from programs, and we are not that far from the point where Social Security and Medicare are 50 percent of the Federal budget, then you would be talking about changes in Social Security and Medicare, among other programs, that are probably well beyond what the public would be willing to accept.

I note that at the beginning of the Entitlement Commission's deliberations, Senator Danforth, a very thoughtful member, as you know, a colleague of yours, said that revenues were off the table. We wanted to get there entirely by spending, but by the time the commission had deliberated for 5 or 6 months, Senator Danforth concurred that the kind of changes one would need by the year 2030 were so great that they ought to include some revenue increases, as well as spending cuts, with the majority being spending cuts. The package he put together did that, but it would be vir-

tually impossible to move on something like that with a two-thirds requirement.

All the major deficit reduction measures enacted between 1982 and 1993, all four of them, three of them signed by a Republican President, did not get a two-thirds margin. The 1983 Social Security rescue plan, strongly supported by President Reagan, did not get a two-thirds margin on the House floor. A proposal that I think makes a lot of sense that a number of Members of both parties are now talking about, scaling back cost of living adjustments tied to the Consumer Price Index—because that affects spending and revenues, that would require two-thirds. It is hard enough to get a majority for it. I don't see it ever happening if we need two-thirds, but those are the kinds of steps I think we will need in the decades ahead.

I am also concerned about corporate subsidies in the tax code, some of which make sense and some of which are the result of special interest pressure. Before the Entitlement Commission, Chairman Greenspan referred to some of those provisions as tax entitlements and urged the commission to look at those as well as spending entitlements in seeking to reduce the deficit.

But, in fact, if we have a two-thirds constitutional limitation, we could get to the situation where Congress passed a series of tax changes it thought were deficit-neutral, clever lawyers and accountants working for people who can afford them found ways to convert some of them into tax shelters and the Treasury lost money, and it would take a two-thirds vote just to get those provisions of the code back to the deficit-neutral situation they were intended to have.

The final point I wanted to make is about Social Security and Medicare. Some of the changes that we need here would run afoul of the two-thirds limitation. For example, both of you voted for a reconciliation bill last year that has a provision I also think is wise to increase Medicare premiums for people at higher income levels who can afford to pay more.

Because the higher premium would be tied to income, the House parliamentarian advised when the measure was about to come to the House floor in November of last year that it could be viewed as a tax increase. That would probably require two-thirds. There, again, we haven't been able to get it into law yet. I don't see something like that ever happening if you need two-thirds.

Similarly, Republicans in both Houses and some Democrats have for a number of years supported wise measures to make all State and local employees subject to Social Security and Medicare. Virtually all of them end up getting Social Security and Medicare when they retire, but some pay in less than their fair share during their working years.

I believe that it was due to people such as former Chairman Rostenkowski that that measure in Senate Republican reconciliation bills of the early 1980's didn't fully become law. Yet, because it would increase payroll tax revenues, it would be subject to two-thirds as well and would probably never occur.

A final point I would just like to make is that if we effectively cannot do things like means-test Medicare benefits, close unproductive special interest loopholes and the like, that will drive us both,

I think, to higher deficits than we would otherwise have over time and to having to go more deeply into things like Medicare across the board, student lunches, student loans, other programs that benefit the middle class and the poor, and that the relative balance of sacrifice in the decades ahead as we balance the budget will be too heavily tilted toward the middle class and the poor if we take off of the table both some of the subsidies that go through the tax code to people at higher income levels and the ability to restrain some spending entitlements by adding means-tested elements into them that would be classified as revenue increases because they are tied to income.

Thank you.

Senator BROWN. Thank you. You have brought some excellent items for discussion to our attention.

[The prepared statement of Mr. Greenstein follows:]

PREPARED STATEMENT OF ROBERT GREENSTEIN

I appreciate the opportunity to testify before the Subcommittee today. I am Robert Greenstein, executive director of the Center on Budget and Policy Priorities. The Center is a non-profit policy institute that specializes on fiscal policy issues at both federal and state levels.

Mr. Chairman, I would like to discuss why I believe a constitutional amendment requiring a two-thirds vote by the House and Senate for any bill raising revenues is unwise. Such an amendment would be ill-advised for several reasons.

- The nation will face very large deficits in coming decades if we maintain current entitlement and tax policies. In 1994, the Bipartisan Commission on Entitlement and Tax Reform forecast that due largely to pressures resulting from the retirement of the baby boom generation, the budget deficit is expected to exceed 15 percent of the Gross Domestic Product (the basic measure of the size of the U.S. economy) by 2030 if current policies are not changed. Many experts believe we will need to consider strong deficit reduction measures that include both spending cuts and revenue increases in the decades ahead.
- The proposed constitutional amendment, however, would effectively preclude such action. The amendment would make it virtually impossible to amass the two-thirds majority required to pass deficit reduction packages that include both reductions in federal programs and measures to raise revenue. The amendment would erect serious new barriers to deficit reduction.
- Furthermore, the amendment would skew fiscal policy in ways that inequitably benefit the wealthiest and most powerful at the expense of the rest of the U.S. population. A two-thirds majority would be required to curb special interest tax expenditures, which disproportionately benefit those at high income levels. By contrast, a simple majority vote would be required to cut federal programs, which primarily benefit the middle class and the poor. Decisions as to how to shrink the deficit and apportion the sacrifice would not be made on a level playing field.
- Finally, the amendment undermines the basic principles of majority rule that are at the heart of American democracy.

I. THE CONSTITUTIONAL AMENDMENT AND THE LONG-TERM FISCAL FORECAST

The federal deficit now has been reduced to two percent of the Gross Domestic Product (the basic measure of the size of the U.S. economy), a level that many economists believe does not cause significant damage even if maintained over a substantial period of time. But as the Bipartisan Commission on Entitlement and Tax Reform warned in 1994, if no action is taken to raise revenue or restrain Medicare, Social Security, Medicaid, and some lesser entitlements—and other federal spending remains constant as a share of GDP—the deficit will rise sharply when the baby boom generation retires. The Entitlement Commission forecast the deficit will exceed 15 percent of GDP by 2030 if no such action is taken. Based on a recent slowdown in the rate of growth of health care costs, current forecasts are a bit less pessimistic, but not by much. President Clinton's new budget forecasts the deficit will equal 12 percent of GDP in 2030 under current tax and entitlement laws and rise further to 26 percent of GDP by 2050. In short, any reasonable long-term forecast will show projected deficits in the next century to be extremely large and of a magnitude unhealthy for the U.S. economy. To avoid such a development, major deficit

reduction that extends far beyond the steps Congress and the Administration are currently considering will ultimately be needed.

Testifing before the Entitlement Commission in 1994, Robert Reischauer, then the director of the Congressional Budget Office, observed that the public would be unlikely to accept the steps that would be required either to extract all of the needed deficit reduction in the decades ahead just from government programs or to extract all of the needed deficit reduction just from revenues. In the long run, Reischauer predicted, policymakers will agree on some mix of program cuts and revenue increases to prevent deficits of a magnitude that would do substantial damage to the economy.

The proposed constitutional amendment is designed to ensure that virtually none of those future deficit reduction measures come from the revenue side and virtually all come from cutting programs.[1] That the amendment would bar virtually all revenue increases can be seen by examining House votes for the four principal deficit reduction measures enacted between 1982 and 1993 that raised federal revenue. Although three of these four measures were signed by Republican presidents and all four enjoyed the support of Democratic Congressional leaders, none received two-thirds support on the House floor. A fifth measure—the 1983 Social Security rescue plan, which increased Social Security payroll tax collections—also failed to secure a two-thirds vote despite strong support from President Reagan and Congressional leaders.

VOTES FOR RECENT LEGISLATION THAT RAISED TAXES

Between 1982 and 1993, five pieces of legislation that raised significant revenue were enacted. Presidents Reagan signed three of these measures, while President Bush and President Clinton each signed one. All five failed to secure a two-thirds vote on the House floor.

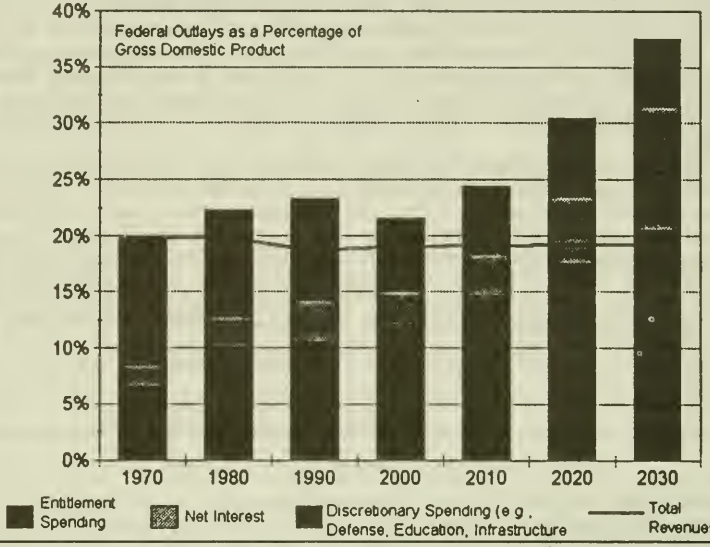
In passing the Tax Equity and Fiscal Responsibility Act of 1982, a measure crafted in substantial part by Senator Bob Dole, the House vote was 226–207. When the House considered its version of the 1983 Social Security rescue plan the following year, the vote was 282–148. The vote for the 1987 budget reconciliation bill, a product of bipartisan negotiations that contained both spending cuts and revenue increases, was 237–181, while the 1990 budget agreement passed by only 228 to 220. The 1993 budget agreement passed by a slender 218–216 vote.

During this period only one measure that raised revenue secured a two-thirds vote, the 1989 reconciliation bill. The 1989 bill was a minor measure. It did relatively little to reduce the deficit and contained only very small revenue increases. The revenue increases in all five of the pieces of legislation that failed to secure a two-thirds vote exceeded the level of revenue increases in the 1989 bill.

The constitutional amendment thus would likely lead to one of several outcomes: (1) larger deficits over time; (2) a greatly shrunken federal government that is unable to do much beyond running Social Security and Medicare, maintaining national defense, making federal pension and veterans payments, and paying interest payments on the national debt; and (3) steep reductions in Social Security and Medicare that significantly reduce the living standards of millions of elderly people who are not well off. Such stark outcomes are not necessary if a balance of spending cuts and revenue-raises ultimately can be considered over the next three decades. Such balance is what the amendment is designed to prevent.

That the statements in the previous paragraph are not hyperbole can be seen by examining a chart the Entitlement Commission published in 1994 showing the fiscal forecast through 2030 under current tax and entitlement law. When the baby boom generation reaches retirement and an unprecedented proportion of the population is elderly, some increases in revenues are likely to be needed, in addition to actions to restrain Social Security and Medicare costs and actions of the type the President and Congress are proposing for the years between now and 2002.

[1] The constitutional amendment would require a two-thirds vote in each House to enact legislation that, in net, increases "internal revenue." While that phrase is ambiguous, it should be noted that the Internal Revenue Code covers individual and corporate income taxes; Social Security, Medicare, and other social insurance taxes; most excise taxes such as those on gasoline, alcohol, and tobacco; and gift and estate taxes.



Source: Bipartisan Commission on Entitlements and Tax Reform; the projected deficit is the amount by which the vertical bar showing federal outlays exceeds the horizontal line showing federal revenues.

II. THE AMENDMENT EFFECTIVELY BARS MEASURES TO CLOSE TAX LOOPHOLES

The requirement for a two-thirds majority would apply not only to measures to raise tax rates but also to measures to cut unproductive tax expenditures that grant subsidies to powerful special interests. A recent Congressional Budget Office study found that over half of the corporate subsidies the federal government provides are delivered through the tax code. Curbing corporate welfare provided through the tax code is one way to help reduce the deficit, but it would require a two-thirds vote under the proposed amendment. This would essentially rule out closing corporate loopholes as a way to help shrink the deficit.

In fact, a substantial share of the federal budget would effectively be placed off limits for deficit reduction by the constitutional amendment. Provisions of the tax code that the Joint Committee on Taxation classifies as "tax expenditures"—spending programs that operate through the tax code by selectively reducing the tax liability of particular individuals or businesses—now cost more than $400 billion a year. (The corporate subsidy provisions that operate through the tax code are a part of this total.) This is more than the government spends on Social Security or defense.

In testimony before the Entitlement Commission in 1994, Federal Reserve Board chairman Alan Greenspan referred to these provisions of the tax code as "tax entitlements" because they entitle those who qualify for them to government subsidies provided in the form of a tax reduction. Greenspan testified that the tax entitlements should be looked at, along with the spending entitlements, in developing measures to address the nation's long-term deficit problem.

MOST STATES DO NOT HAVE SUPERMAJORITY REQUIREMENTS

Only six states require the approval of at least two-thirds of their legislatures for any tax increase. Five other states either require such approval for some taxes but not others, require a three-fifths rather than a two-thirds vote, or both. Other states generally require simple majority approval for revenue increases of all sorts.

Furthermore, a 1993 General Accounting Office study of state budget trends found that a majority of states surveyed had used both spending cuts and revenue in-

creases to balance their budgets in recent years. Revenue increases accounted for about one-third of the deficit reduction these states instituted to balance their budgets during the period studied.

If anything, the proposed constitutional amendment would encourage the spread of more tax expenditures over time, since such measures would take only a majority vote to enact but a two-thirds vote to remove. In addition, if Congress passed a series of tax changes that were thought to be deficit-neutral, but clever, high-priced tax lawyers and accountants then found ways to convert some of the measures into tax shelters at greater-than-anticipated cost to the Treasury, it would take a two-thirds vote to scale the shelters back so the original measure did not produce a net revenue loss.

Even measures that raised revenue by shutting down opportunities for tax fraud would require a two-thirds vote. So would measures to tighten tax procedures so billionaires who made their fortunes in the United States did not move abroad and become expatriates to avoid paying their fair share of taxes. So also would measure to prevent companies from gaining tax advantages by moving plants—and jobs—overseas.

III. AMENDMENT TILTS TOWARD THE WEALTHY AND THE POWERFUL AT THE EXPENSE OF AVERAGE FAMILIES AND THE POOR

Most government benefits that low- and middle-income Americans receive come from government programs, such as Social Security, Medicare, Medicaid, student loans and grants, unemployment insurance, school lunches, and food stamps. By contrast, most government subsidies that wealthy individuals and large corporations receive come through tax subsidies. As a result, a constitutional amendment that makes it extremely difficult to scale back tax subsidies when decades of deficit reduction lie ahead tilts the playing field in favor of the wealthy and powerful over Americans of average or lesser means.

In addition, such a constitutional amendment would place off-limits even measures asking program beneficiaries who have high incomes to pay more for the government benefits they receive. For example, measures to "means test" Medicare premiums by raising the premium charges for those at high income levels must rely on the tax code to collect the increased premiums, since Social Security offices (which administer Medicare) have no information on beneficiaries' current incomes. Indeed, when the Republican budget bill reached the House floor last fall, the House parliamentarian advised that its provision raising Medicare premiums for those at higher income levels could constitute a tax increase. Under the constitutional amendment, measures of this nature would require a two-thirds vote, rendering them extremely difficult to pass. This makes it more likely that when steps are taken to restrain Medicare costs, low-income and middle-income beneficiaries will have to bear a heavier share of the load.

LAW SCHOOL DEAN WARNS OF PERVERSE EFFECTS

In testimony before the Subcommittee on the Constitution of the House Judiciary Committee on March 6, Samuel C. Thompson, Jr., Dean of the University of Miami Law School, warned of potential perverse effects from the proposed amendment. Thompson wrote:

> * * * adoption of this proposed amendment would significantly penalize the American public for mistakes made in the tax legislative process. For example, assume that after adoption of this Constitutional amendment, Congress adopts a flat tax. Assume that it is estimated that the flat tax will reduce revenues by $100 billion. It turns out, however, that tax lawyers discover a gaping hole in this legislation and that as a result the revenue loss is $200 billion, not $100 billion. The Treasury immediately proposes a base-broadening amendment to close the loophole and to restore fiscal responsibility. The amendment is opposed by powerful special interests who will prevail if they can convince just 33⅓ percent of the members of either the House or the Senate to vote against the amendment.

The amendment also would be likely to injure the middle class and the poor for another reason. If the federal government is unable to raise revenue when needs for public expenditures rise, one likely result will be to shift more of the burden of raising revenue and meeting public needs to state and local governments. Most state

tax codes are regressive (i.e., the taxes they impose consume a larger percentage of the income of lower-income households than of higher-income households). State and local governments extract a larger proportion of the revenues they raise from the middle class and the poor, and a smaller proportion from the affluent, than the federal government does. If revenue-raising burdens are shifted from the federal to state and local levels, the share of the overall tax burden borne by the middle class and the poor is likely to rise.

IV. AMENDMENT COULD LEAD TO OVERLY LARGE CUTS IN SOCIAL SECURITY AND MEDICARE BENEFITS

Social Security and Medicare benefits need to be restrained in the years ahead. Both programs are out of long-term actuarial balance, and both contribute significantly to the projected increase in the long-term deficit.

But the constitutional amendment would almost certainly lead to larger reductions in Social Security and Medicare benefits than otherwise would be needed, reductions that could adversely affect the living standards of modest-income or poor retirees. This would be true for several reasons.

First, by effectively preventing revenues from contributing to deficit reduction despite the need for large-scale deficit reduction in the decades ahead, the amendment would place a greater deficit reduction load on Medicare and Social Security. These two programs are projected eventually to constitute half or more of the federal budget, exclusive of interest payments on the debt. If there is no revenue contribution to deficit reduction, there will have to be a greater contribution from Medicare and/or Social Security than would otherwise be the case.

Second, the amendment would effectively rule out measures to raise Medicare premiums for those at higher income levels. As noted above, last year's budget reconciliation bill contained such a measure. When it was about to come to the House floor, the House parliamentarian advised that it could constitute a tax increase. A House rule that the new Congress adopted in January 1995 requires a three-fifths majority for measures raising tax rates, so the parliamentarian's advice meant the budget bill would need a three-fifths vote unless this rule was waived. The House leadership promptly arranged for a waiver of the rule. But once a supermajority requirement is in the Constitution, no waivers are possible.

Third, the constitutional amendment effectively rules out even small adjustments in Medicare and Social Security payroll taxes as part of the effort to bring these programs into long-term actuarial balance and also help reduce the deficit. Modest increases of a fraction of a percentage point in the payroll tax would require a two-thirds vote, thereby making them virtually impossible to achieve. Yet Medicare in particular is so far out of actuarial balance that it is difficult to see how to restore long-term balance to the program without some increase in payroll tax contributions along with other changes, unless the health insurance that Medicare provides is scaled back substantially.

In a symposium last September, Henry Aaron, Director of Economic Studies at the Brookings Institution and a well-known expert in this area, observed that the full $270 billion that Republican Congressional leaders were seeking in Medicare savings over seven years could be achieved if one combined Republican Medicare proposals that represent sound policy and yield about half of the $270 billion in savings with an increase of one-quarter of one percentage point in the employer and the employee shares of the Medicare payroll tax. This would slightly reduce workers' wages. (Most economists believe that both the employee and the employer shares of payroll taxes are effectively borne by employees in the form of wages lower than they otherwise would be paid. As a result, claims that small increases in payroll taxes would heavily burden employers and cause substantial job loss have little merit.) In return, employees would get a Medicare system that had the resources to provide continually improving health care to their parents and ultimately to themselves as it took advantage of emerging medical technologies that improve health and prolong life.

Furthermore, one of several reasons that Medicare and Social Security face long-term deficits is that over time, a steadily increasing share of employee compensation is being provided in the form of fringe benefits not subject to the payroll tax, while a steadily smaller share is provided in wages that are subject to the tax. Modest measures to shore up Social Security and Medicare by slowing the erosion in the share of employee compensation subject to the payroll tax would, however, also require a two-thirds majority.

Even measures to bring all state and local government employees into the Social Security system—a step nearly all budget analysts favor regardless of whether they are conservative or liberal, and which would strengthen the Social Security system

and reduce the deficit—would require a two-thirds vote, because such measures would increase federal revenue. Such measures would become virtually impossible to pass. (For a further discussion of these issues, see an accompanying Center on Budget and Policy Priorities analysis, "Proposed Constitutional Amendment Would Make It More Difficult to Address the Long-Term Social Security and Medicare Crises.")

V. WEAKENING OUR SYSTEM OF DEMOCRACY

Finally, the amendment would gravely weaken the principle of majority rule that has been at the heart of our system of representative democracy for more than 200 years. As Rep. James Moran has observed, it would partially restore the system we had in the 1780s under the Articles of Confederation, a system that functioned poorly and was soon scrapped.

The Articles of Confederation required the vote of nine of the 13 states to raise revenue. At the Constitutional Convention in 1787, the Founding Fathers recognized this was an insurmountable defect and fashioned a national government that can impose and enforce laws and collect revenue through simple majority rule.

The proposed constitutional amendment would end the ability of a majority of the American people, acting through their duly elected representatives, to decide whether they would like to raise more revenues so the federal government can address needs the majority finds legitimate. The amendment would deny the majority this right both now and in future generations.

JAMES MADISON ON MAJORITY RULE

The Constitutional Convention rejected requiring supermajority approval for basic functions such as raising taxes. Supermajority rules had applied in the Continental Congress. The framers of the constitution had experience with these rules and understood what they were rejecting.

In the Federalist Papers No. 58, James Madison, one of the key figures in drafting the Constitution, explained why the Constitution rejected supermajority rule:

> It has been said that more than a majority ought to have been required for a quorum, and in particular cases, if not in all, more than a majority of a quorum for a decision. * * * [But that would mean] * * * [i]n all cases where justice or the general good might require new laws to be passed, or active measures to be pursued, the fundamental principle of free government would be reversed. It would be no longer the majority that would rule; the power would be transferred to the minority. Were the defense privilege limited to particular cases, an interested minority might take advantage of it to screen themselves from equitable sacrifices to the general weal, or in particular emergencies to extort unreasonable indulgences."

Madison equated majority rule with "free government." In his view, freedom consisted not just in protecting individuals from unreasonable intrusion by government, but also in the right of citizens to have an equal voice in the affairs of government. According to Madison, a person whose vote is diluted by supermajority rules is not an equal citizen and so does not fully enjoy the fruits of freedom.

At its core, the amendment is rooted in deep distrust of the ability of the majority of the American people to make decisions that the authors of the amendment believe to be ideologically correct. Hence, the amendment seeks permanently to deny the majority that right. Powerful, well-connected minorities would gain great power at the expense of the majority. In short, the amendment fundamentally is anti-democratic.

CENTER ON BUDGET AND POLICY PRIORITIES

April 5, 1996

PROPOSED CONSTITUTIONAL AMENDMENT WOULD MAKE IT MORE DIFFICULT TO ADDRESS THE LONG-TERM SOCIAL SECURITY AND MEDICARE CRISES

The proposed constitutional amendment requiring two-thirds approval by the House and Senate to pass any bill that increases federal revenues would make it more difficult to address the long-term financing problems of Social Security and Medicare. Those financing problems are serious:

• The 1995 report of the Social Security trustees projects the Social Security trust fund will start running deficits by 2011 and exhaust all of its reserves—that is, become insolvent—by 2030.

• The trustees also project that the Medicare Hospital Insurance trust fund will become insolvent in just six years, in 2002.

The resulting trust fund imbalances will be so great that there is a strong possibility they cannot be addressed by benefit cuts alone. To do so would likely require Social Security and Medicare benefit reductions so severe that they go beyond what the American public would accept. In 1994, a panel of Social Security experts—two Republicans and two Democrats—testified before the Kerrey-Danforth Entitlement Commission. The experts unanimously agreed that both benefit restraint and additional trust fund revenues would be needed.

Some Members of both parties believe that one way to help address the looming shortfalls in Medicare and Social Security is to scale back benefits for those at high income levels. For example, the budget reconciliation bill that Congress passed in November 1995 (and that President Clinton subsequently vetoed) would have increased the premium charged for Medicare Part B (physicians' services) to those at higher income levels. But measures such as this entail raising revenues. Social Security offices, which administer Social Security and Medicare, have no information on beneficiaries' current incomes. The only practical and efficient way to scale back benefits for high-income beneficiaries is to use the tax system to recover a portion of the benefits. To attempt to do so without using the tax system would require hiring a legion of new bureaucrats to staff Social Security offices and collect information on beneficiaries' incomes.

Indeed, when the Republican budget bill reached the House floor last fall, the House parliamentarian advised that its increase in Medicare premiums for those at higher income levels could constitute a tax increase. Since House rules adopted in January 1995 require a three-fifths vote on the House floor for measures raising tax rates, the parliamentarian's advice meant the budget bill needed a three-fifths majority, unless the three-fifths rule was waived. The House Rules Committee provided a waiver of the three-fifths rule; the bill passed by majority vote but did not receive a three-fifths vote. If a supermajority requirement is enshrined in the Constitution, however, no such waivers will be possible. Measures to means-test the Medicare premium to strengthen Medicare's finances and simultaneously reduce the deficit will become far more difficult to pass.

Still another example of the problems the constitutional amendment would cause can be seen by examining a measure recommended unanimously by the Social Security experts panel that appeared before the Entitlement Commission. The panel called for covering all state and local government employees under the Social Security system. State and local government employees in certain states are the only substantial group of workers not now covered by Social Security. Expanding coverage to this group would likely benefit many workers who spend only part of their careers in the government sector and would improve the balance in the Social Security trust fund. But expanding coverage is a revenue increase because the newly covered employees and their state and local employers would become subject to the Social Security payroll tax.

Requiring a two-thirds vote for measures such as these would make it far harder to address long-term Social Security and Medicare financing problems without imposing deep benefit cuts on low- and middle-income beneficiaries.

The experience of the Entitlement Commission is instructive in another way as well. Mostly because of the trust fund imbalances and the growth of other federal health care entitlements, the Commission projected that by 2030, the deficit would exceed 15 percent of the Gross Domestic Product (GDP). In a more recent projection, the Office of Management and Budget has estimated the deficit will be 12 percent of GDP in 2030 and rise further to 26 percent by 2050. By contrast, the current deficit is two percent of GDP.

To erase deficits of this magnitude, extraordinary actions will be needed in future decades. Doing the entire job by cutting government programs is likely to require draconian changes deemed unacceptable by the public. Indeed, although Senators Kerrey and Danforth explicitly ruled out revenue increases at the first meeting of the Entitlement Commission, by the last meeting their view had changed. Their recommendations contained a number of proposals that would increase revenues to help tame the long-term deficit, along with very tough reductions in entitlement benefits. Their revenue proposals included: covering state and local employees in the Social Security system; capping the tax deduction for employer-paid health insurance; limiting the marginal tax rate against which itemized deductions may be taken to 28 percent; and adjusting the indexing of tax brackets, the standard deduc-

tion, and other elements of the tax code for inflation based on an index other than the current CPI.

ENDLESS LITIGATION

Finally, the proposal raises difficult issues that would probably need to be resolved by the Supreme Court. For example:

- Is a bill that increases revenues in some years but decreases them in others (and decreases them over a multi-year period) unconstitutional if it does not secure a two-thirds vote?
- What if a bill is thought to reduce revenues but turns out actually to raise them? Is that law unconstitutional? Are refunds due?
- What if certain "supply side" arguments are right, so that in some cases a cut in tax rates will increase revenues. Does that render the measure unconstitutional unless it gets a two-thirds vote?

Senator BROWN. Dr. Niskanen with the Cato Institute, one of the best-known and well thought of think tanks in Washington. We appreciate your coming.

STATEMENT OF WILLIAM A. NISKANEN

Mr. NISKANEN. Thank you, Senator Brown. I am privileged to testify in support of an amendment that would require a supermajority to increase Federal taxes, and I am honored that Senator Kyl has chosen to adopt the language and the voting rule that I have long proposed as part of a balanced budget tax limitation amendment.

My written remarks address four or five different issues. I want to focus my oral remarks, really, on two issues. No 1, is the language of the amendment. My suggested wording of the tax limit amendment as section 1 of the proposed amendment is designed to serve two objectives. No. 2, is the limit is expressed in terms of the explicit provisions of a tax bill rather than on some analyst's necessarily controversial forecast of whether the bill would increase total tax revenues.

It is much too much of a burden for an employee of Congress to have to tell his or her superiors that a specific bill would require a supermajority vote to pass. Just from an administrative reason, I think that a limit expressed in terms of revenues is less likely to be enforceable.

More important, the wording would also provide considerable stability to the details of the tax code, an objective that is not achievable by a revenue limit. This wording, one should recognize, would require a broader coalition to make both good changes and bad changes in the tax code. For that reason, some advocates of tax reform may prefer deferring a tax limit amendment until a preferred tax reform has been approved. I suggest that this would be a mistake. Broad bipartisan support is a necessary condition of enduring tax reform and the proposed wording would weed out those proposals least likely to survive.

Now, from a timing point of view, it will take several years, maybe half a dozen years or so for final approval of a constitutional amendment, and I think putting a constitutional amendment in the start of that process is likely to increase or accelerate the process of getting tax reform. So I don't regard tax reform and an effective amendment to be in competition.

Second, on the question of the voting rule, my very strong preference is to package a tax limit amendment with a balanced budget

amendment, and the same voting rule should be required to increase taxes and to increase the debt. If you have a two-thirds rule on taxes and a three-fifths rule on the debt, for example, you strongly bias fiscal decisions in favor of increased borrowing rather than increased taxes. This consideration by itself leads me to prefer the three-fifths rule that is included in the balanced budget amendment already approved by the House and within a vote or two of being approved by the Senate.

Third, from a more general point of view, the voting rule on fiscal totals should be higher, the larger is the difference between the mean and the median tax burden per household. It is that difference between the average or the mean and the median tax burden that is the primary origin of the bias in fiscal decisions in a democratic government.

My recent study of the fiscal choices in a democratic government lead me to conclude that a three-fifths voting rule would be sufficient to offset the bias resulting from the progressivity of our current tax code. Now, in detail, what that means is that a three-fifths voting rule looks like it would achieve roughly the same outcomes as if we had a strictly proportional tax system, in which case the mean and the median tax rates would be the same. So I think that going beyond a three-fifths rule is not necessary to offset that bias.

In summary, I have changed my mind since I first supported a two-thirds rule on taxes. I now conclude that a three-fifths rule is better than a two-thirds rule, as well as I think being more acceptable politically. Again, I encourage you to consider a tax limitation amendment as part of a broader balanced budget tax limitation amendment in which the same supermajority rule should be applied to both the decisions to borrow and a decision to increase taxes.

Thank you.

[The prepared statement of Mr. Niskanen follows:]

PREPARED STATEMENT OF WILLIAM A. NISKANSEN

Mr. Chairman and members of the subcommittee: I am privileged to testify in support of an amendment to the Constitution that would increase the congressional majority necessary to increase federal taxes. And I am honored that the sponsors have chosen to adopt the language and voting rule that I have long proposed as part of a balanced budget/tax limitation amendment.

My testimony today briefly addresses four issues:

1. The case for a tax limit amendment should now be obvious. The original design of our Constitution was to limit the powers of the federal government to those enumerated in Article 1, Section 8. Although there was some breach of these limits from the earliest years, they were remarkably effective for 140 years; in 1929, for example, the federal budget was 2.6 percent of GDP, most of which was spent for the military and the deferred costs of prior wars. Any limits on the spending powers of the federal government, however, effectively disappeared during the New Deal, a constitutional revolution that was ratified by a compliant Court. Since then, the federal budget has grown to nearly 23 percent of GDP, without one amendment that would authorize the many additional new spending programs. In some abstract sense, it may be better to limit the spending powers than to limit the total taxing and borrowing authority, but that genie is already out of the bottle. A balanced budget/tax limitation amendment may be a second best approach but one that is now necessary to counter the erosion of the constitutional limits on the spending powers.

2. My suggested wording of a tax limit amendment, incorporated as Section 1 of the proposed amendment, is designed to serve two objectives:

• The limit is expressed in terms of the explicit provisions of a tax bill, rather than on some analyst's controversial forecast of whether the bill would increase total tax revenues.

• This wording would also provide considerable stability to the details of the tax code, an objective not achievable by a revenue limit.

This wording, one should recognize, would require a broader coalition to make both good and bad changes in the tax code. For that reason, some tax reform advocates may prefer deferring a tax limit amendment until their preferred tax reform has been approved. I suggest that this would be a mistake. Broad bipartisan support is a necessary condition of an enduring tax reform, and the proposed voting rule would weed out those reform proposals least likely to survive.

3. Two considerations bear on the choice of a voting rule:

• My strong preference is to package a tax limit amendment with a balanced budget amendment, and the same voting rule should be required to increase taxes and to increase the debt. This consideration leads me to prefer the three-fifths rule included in the balanced budget amendment approved by the House.

• In general, the voting rule on the fiscal totals should be higher the larger is the difference between the mean and the median tax burden per household. My recent study of the fiscal choices of a democratic government leads me to conclude that a three-fifths voting rule would be sufficient to offset the bias resulting from the progressivity of our current tax code.

In short, I have changed my mind since my first support of a two-thirds rule on taxes. I now conclude that a three-fifths rule is better than a two-thirds rule, as well as being more acceptable politically.

4. The other language of the proposed amendment seems unduly wordy and inelegant. My strong preference is to permit Congress to waive the tax rule only upon a declaration of war. Our government should not engage "in military conflict which cause an imminent and serious threat to national security" without a declaration of war. And Section 3 could be replaced by adding the few words "by a roll call vote" to the end of Section 1. But these are minor issues.

My thanks for your attention. I have been studying, drafting, and promoting tax limit amendments at both the state and federal level for over 20 years, and I am pleased to see the interest and increasing support for an effective federal tax limit.

Senator BROWN. Thank you.

Senator Kyl.

Senator KYL. Thank you, and I thank all of the panelists here for their comments. I especially want to compliment Grover Norquist. By the way, I will pronounce that name again for the record. My colleague from Wyoming has on occasion mispronounced it, but Grover Norquist heads up a group called Americans for Tax Reform which has put out an incredibly informative and thorough report called "Growth, Prosperity and Honest Government: The Case of Constitutional Tax Limitation."

This particular document has a great deal of information about the impact of taxes on our lives, and the case for an amendment like this. I really suggest that anyone interested in this subject needs to read this. My staff has written on the front of this, "This is the bible on this subject," and I think that my staff is correct with regard to that.

I also want to compliment my colleague from Arizona, my successor in the House of Representatives, John Shadegg, who noted at the beginning of his comments that he was very much involved in the drafting of the language requiring a two-thirds supermajority to raise taxes in the State of Arizona. He and his colleagues were very careful to consider all of the various technical objections, and in the end I think he agreed with Grover Norquist that it boils down to whether you are going to focus on the things that make it hard or you are going to focus upon the need for it. In the end, as he said, over 70 percent of Arizona voters said, we are not so

concerned about the details; it is time to stop raising taxes as much as you do; let's make it harder to raise taxes.

With regard to the debate about three-fifths or two-thirds, I guess I would argue that we ought to make both debt-raising and tax-raising two-thirds rather than three-fifths, but let's leave that issue aside. The question that I would really like to ask Dr. Niskanen and Grover Norquist has to do with the difference between the version of the legislation introduced here in the Senate and that which the House will be voting on, and then I do also have a question for Mr. Greenstein at the end.

The Senate language is really very simple and straightforward. "Any bill to levy a new tax or increase the rate or base of any tax requires a two-thirds majority." Then there are exceptions for declarations of war, and so on. In the House version that will be voted on, in an effort to gain wider appeal, the language was watered down significantly and now focuses on a different concept, the concept of revenue neutrality, a concept which in my mind begins to permit the worst of all worlds, which is as long as we collect the same amount of revenue we can redistribute the burden among those who pay.

In addition to that, of course, are the arguments that three of you have made that it is going to be pretty difficult to figure out what is tax-neutral. I think Mr. Greenstein pointed that out as well. Moreover, sometimes tax cuts provide more revenue. In fact, frequently that is the case, so trying to figure out whether a proposal is going to be revenue-neutral or not seems to me to be a pretty difficult task.

I wonder if you could all speak to the issue, particularly Dr. Niskanen and Grover Norquist. Which of these two provisions, the House or Senate provision, is likely to result in greater difficulty to raise taxes and whether there are difficulties in interpretation, or relative difficulty of interpretation between the two different proposals.

Mr. NISKANEN. Senator Kyl, I very strongly prefer your version. It is the same language that I have recommended as part of the balanced budget tax limitation amendment now for some years. It does two things. First, is that I think it is very much easier to administer than a revenue limit. The second is that it does provide some stability to the details of the tax code. It reduces the opportunity for redistribution of the tax burden within a given amount of revenue.

I think both of those objectives are desirable, as the revenue limit itself puts the head of the Joint Tax Committee or the head of CBO or somebody in an extraordinary position of having to tell her boss, I am sorry you have to have a two-thirds vote on this issue rather than a majority.

Senator KYL. An extraordinarily powerful position, really.

Mr. NISKANEN. What?

Senator KYL. An extraordinarily powerful position, as well.

Mr. NISKANEN. An extraordinarily powerful two-thirds, and I think that is too much of a burden to place on an employee of Congress. I think it is very much more straightforward to express the limit in terms of the detailed content of the bill without requiring a revenue forecast. Second, I think it is desirable in and of itself

to provide some stability to the details of the tax code, for the fact that I recognize that there is an awful lot of junk in the tax code. There is a very strong case for major tax reform. I think that some stability in the tax code is desirable in and of itself.

Senator KYL. Grover Norquist.

Mr. NORQUIST. I concur. The language that the Senate is proposing that you have proposed is superior to the final version that the House is talking about. The good news is that this amendment is not passing today, tomorrow, or next week. Many of the people in the House of Representatives who will be cheerfully voting for the Barton-Shadegg-Geren-Hall amendment also share the view that the original language and language closer to your version in the Senate is preferable.

I think this is an educational campaign both on Capitol Hill and around the country, and so I am not as troubled by the less good language in the House as I might be if I thought this was all going to be wrapped up next week. We have time to educate the public, the House and the Senators, and I think it may take us another election to have in the House and the Senate two-thirds of both bodies that, when they talk about budgets, think about the family budget rather than the Federal budget and when they talk about taxes think of it as an outgo and a cost rather than a revenue and income.

Senator KYL. Thank you. Mr. Chairman, I see my time is expired. May I just make two quick comments? No. 1, I know that Representative Shadegg shares the view that if we could it would be better to go with the Senate version, but in order to bring this matter to attention and get it to a vote was willing to make some concessions at least for now. But at the point in time when we believe this is really going to be the final language, I hope we get much closer to the Senate version.

Mr. Chairman, I just wanted to make a point, and Mr. Greenstein certainly could respond to this if he wishes, but I would like to make one point with respect to his comments. His very beginning comment was that in order to ensure fiscal soundness of our budget, there should be a combination of spending cuts and revenue increases.

I know that it is almost impossible for people to say "tax increases." Tax increases, of course, are not the same as revenue increases. In fact, by reducing taxes, we can frequently increase revenues, as Governor du Pont pointed out. I think that the primary point, though, and the issue that you raised regarding revenue neutrality does argue more for the Senate version as opposed to the current House version of language if one wanted to achieve this objective by constitutional amendment. Would you agree with that?

Mr. GREENSTEIN. Actually, I would not.

Senator KYL. You prefer the revenue neutrality that——

Mr. GREENSTEIN. I share the concerns that Grover Norquist and particularly Bill Niskanen made, and you also, about the revenue neutrality and the scoring issues, and I think I mentioned some of that in my testimony. I must say I am even more troubled by the Senate language, and this is not on deficit reduction grounds but on tax policy grounds.

What I don't understand, for example, is why would one want to have a two-thirds limitation for something like the 1986 Tax Reform Act. I happen to think the 1986 Tax Reform Act, while far from perfect——

Senator KYL. Now, that passed with a two-thirds majority in both the House and Senate, the 1986 Tax Reform Act, but go ahead.

Senator BROWN. To that point, it was 92.6 percent in the Senate and 74.5 percent in the House.

Mr. GREENSTEIN. But 1986 was an unusual constellation; everything came together. It would be harder in the future to pass other revisions in the tax code that are deficit-neutral and that make improvements in the——

Senator KYL. But it doesn't have to be deficit-neutral. That is really the point I was getting at. Under the Senate language, there is no deficit neutrality concept. See, that is the problem with the current House version.

Mr. GREENSTEIN [continuing]. Let me restate my point.

Senator KYL. All right.

Mr. GREENSTEIN. The 1986 Tax Reform Act or other things like that—I am a big fan of broadening bases, reducing the number of special treatments of this or that and then you set the rates where you want to set the rates. The 1986 Act broadened the base and lowered the rates. I think that was the right way to go. I am not a flat tax fan, but I like the idea of broader bases and lower rates. Whenever you broaden the base, you gore somebody's ox.

In 1986, we did have an unusual constellation of events with both parties aligning on that. I don't know how many times that will happen again in the future and I just have concerns about requiring two-thirds, a much higher hurdle, to do improvements of that nature in the tax code where the bottom line—in the way that, you know, you and others here at the table look at it, the bottom line is that one is not increasing the tax take from the public. One is trying to make the tax code fairer and more efficient, and I have difficulty in requiring a supermajority rather than a majority for proposals to make the tax code more efficient and fairer.

Senator BROWN. Dr. Niskanen.

Mr. NISKANEN. I think you should recognize that there is a very strong complementarity between tax reform and a supermajority. Tax reform unfortunately has become a bit of a bait-and-switch operation. The reformers come along and say let's broaden the base in order to get rates down, and then people like Mr. Bush and Mr. Clinton come along and say, what a great temptation, we have broadened that base, let's just tweak the rates a little bit.

Senator KYL. Upward.

Mr. NISKANEN. And that has made people skeptical, if not cynical, of tax reform. Both Mr. Armey and Mr. Gephardt have recommended that special voting rules accompany their tax reform proposals. Armey has proposed a supermajority of Congress. Gephardt has recommended a national referendum as necessary to override it. So I think that a supermajority is necessary to lock in tax reform so that it is not eroded away within a matter of a few years after the reform.

The top marginal rate in 1986 tax law was 28 percent. It is now about 42 percent. We have increased the top marginal rate 50 percent in 10 years. That kind of increase would not have been possible if a supermajority had been in place. The Clinton tax bill passed with one vote, not two-thirds, and we would still have something much closer to the 1986 tax law if we had a supermajority requirement in place.

Senator BROWN. Thank you. I am just going to take one question. Mr. Greenstein raised a very important point when he talked about the budget crisis that is out in front of us, not just present, but out in front of us, and what I thought was a plea for flexibility in developing an answer to it.

It used to be that we lived in a world where the very wealthy in this country had servants and mansions, where there were huge concentrations of wealth. Obviously, you still have people like Bill Gates and a variety of families that are very wealthy, but my impression is that we are in a different world. The style of concentration of wealth that existed around the turn of the century clearly doesn't exist today.

We have a tax code that used to have over half the Federal income tax come from the top 10 percent income category and the bottom half in terms of income paid something under 10 percent. Actually, that has changed. As Dr. Niskanen has implied, with the change in rates, now the top 10 percent pays significantly more than 50 percent of the Federal income tax and the bottom 50 percent pays significantly under 10 percent.

My impression is the 42-percent rate that you talked about, doctor, is accurate, but does not include Social Security, which would raise that.

Mr. NISKANEN. The top marginal income tax rate is 39.6 and the Medicare tax rate applies to all earnings at any level, and that is another 2.9. So we are in the 42-percent range, including the income tax and the Medicare.

Senator BROWN. In addition, of course, you would have State taxes.

Mr. NISKANEN. That is right. Federal alone is in the 42-percent range.

Senator BROWN. So when you add them together, you are probably at least 50 percent, depending on the State. We are now in a world market that includes not just goods and services, but people as well. I give you that background because you may want to object to the premises from which I approach this. How much more can you get out of the upper-income groups in this country? What is our ability to shift tax burden further, or are further tax increases simply going to come out of the hide of the middle class?

Mr. GREENSTEIN. I think the unfortunate reality, looking at the long-term fiscal forecast, is that both on the benefit and the revenue side I think everybody at all income levels is going to have to sacrifice a bit more. In terms of the income distribution, you are right that it is not as skewed as at the turn of the century. It is more skewed than it was 15 or 20 years ago.

The latest CBO figures that CBO compiled last year showed that in 1992 about the top 20 percent of the population had about 50 percent of the income and that was up from where it had been 20

years before. I should hasten to say this doesn't have anything to do with Ronald Reagan or any policies here. It is basically trends in the international economy.

Senator BROWN. Well, on that point, let me raise a question because you maybe can answer it. My impression is that those numbers are phony as hell.

Mr. GREENSTEIN. No.

Senator BROWN. Let me tell you why. They specifically do not include noncash benefits. Now, if you have a society that provides a wide range of welfare assistance to people and they do a significant portion of it in noncash benefits so that a big portion of the income from the poor is not counted, you are going to have a change in figures because you are not calculating or counting the majority of the income that the poor get in this country.

Mr. GREENSTEIN. There are subsequent analyses that do adjust for non-cash benefits and there are changes, but they are relatively modest. But let me not get into a quibble on that.

Senator BROWN. But when you count the non-cash benefits, doesn't it change the numbers you just gave us?

Mr. GREENSTEIN. Not as much as you would think, but let me not get into a quibble on that and get really to the point you are addressing. Do I favor significantly higher marginal tax rates on people at high income levels? No, but I do think that we need to take a look both in the individual and in the corporate income tax and in other parts of the code at areas where the base can be broadened. I think there are areas that probably disproportionately affect higher-income people more than middle-income people where the base can be broadened.

Having said that, I think that in the middle-income area we also need to look at things like Medicare premiums. I happen to favor the kinds of changes in Medicare premiums that were in the legislation that you all put through last year. I think we have to do all of those things. We have to look at the programs for the poor as well, but let me give you an example that illustrates my concern.

Under the constitutional amendment, if we were to say we think that one of the Government spending programs that provides child care assistance to lower middle-income families, people at $10,000, $20,000, $30,000, somewhere in that range, have too much money and we want to cut them back, a majority vote. If we said we don't think that we need to subsidize the child care of people at $200,000 a year and we are going to phaseout the dependent care tax credit, which is a child care subsidy delivered through the tax code for people at that income level, something Senator Grassley has proposed in the past that I am in favor of, that would require two-thirds.

Both of those are reductions in Government child care subsidies. One subsidy is delivered through the tax code, one subsidy is delivered through a spending program. I think they both should require the same number of votes. That is the kind of point I am trying to make.

Senator BROWN. A very helpful point.

We will take a brief recess now and when we reconvene at 1 o'clock, Senator Kyl will Chair the hearing. We appreciate this panel's comments very much.

Senator KYL. Mr. Chairman, do we have just 2 minutes?

Senator BROWN. Yes, we do have 2 minutes and you have the Chair.

Senator KYL [presiding]. Thank you. I really would appreciate that. First of all, I just wanted to make the point that I—oh, I see. I have the Chair if we have 2 minutes. I understand.

Senator BROWN. You may have much more.

Senator KYL. Let me take a quick pause then to converse with you, but I would like to get back to the panel for one thing.

[Pause.]

Senator KYL. The next panel starts at 1 o'clock and it relates to a somewhat different subject and therefore I did want to conclude with this. I have just always found it difficult to categorize letting people keep more of the money that they earned as a Government subsidy. I understand when you collect money and distribute it to somebody else—let's say that you collect money from Mr. Greenstein and then give it to a farmer not to grow a crop. That is a subsidy.

If the Congress decides that Mr. Greenstein and his family would be better off spending their own money rather than the Government taking it, I find it an astonishing view that that is a subsidy. So, I think, here we need to be very, very careful about the language here. I don't know whether you would disagree with that, but you did, both in the report and in your testimony, refer to that as a subsidy.

Mr. GREENSTEIN. I would disagree with that. I think many economists would, and I think actually people like Alan Greenspan, who referred to some of these as tax entitlements before the Entitlement Commission, would. Let me very succinctly try to explain why.

I understand your point, but let's suppose a particular group of individuals comes to Washington and wants a subsidy. Everybody in its group is supposed to get $1,000 and it can write a law one way that the Government sets up a program and it gives them $1,000—call it a farm subsidy, a poverty program, whatever it may be, a student loan—or it can write its program, its legislation, another way and everybody still gets the $1,000 subsidy for the same purpose to be used in the same way, but instead of the Government giving you a check, you subtract $1,000 from the taxes that would otherwise be owed by everybody else in your circumstance.

Most economists would view both of those as being a $1,000 Government subsidy. One way it is written into the tax code and in another way it is written into a tax program, but it is the same effect. That is the point I am trying to make.

Senator KYL. I submit that conclusion, that attitude, that definitional approach is precisely what is wrong with the Federal Government today. Bureaucrats and economists and politicians have gotten into the habit of thinking that they are doing you a favor when they let you keep more of the money that you earned, and even categorize that definitionally as the same thing as—well, you did; you said it is the same either way, whether you let people keep more of their own money by not taxing it or you take it from someone else and give it to them.

Mr. GREENSTEIN. No, no.

Senator KYL. You said both of those are subsidies.

Mr. GREENSTEIN. Let me clarify.

Senator KYL. Please do.

Mr. GREENSTEIN. Is any reduction in taxes a tax subsidy? Of course not. The Joint Tax Committee and the Congressional Budget Office have long had a specific definition of a tax subsidy. When you lower the rate, you don't give somebody a tax subsidy. What we are talking about here is special treatment to particular categories of people so that they pay less than they otherwise would. I can get, if you would like, for the record the specific——

Senator KYL. Well, no. I understand the point that economists have to have a definition, but I still argue with the premise that when you allow families with children to keep more of their income that that is a subsidy. This is just a definitional argument that you and I have.

Mr. GREENSTEIN. I am not saying all subsidies are bad, but I just would make the point that under its new director, June O'Neill, the Congressional Budget Office issued a study last summer on business subsidies and it classified as business subsidies both a number of direct spending programs, like the market promotion program and others, and a series of tax expenditures. That is what I am talking about. I am not talking about raising or lowering the corporate tax rate. I am just following——

Senator KYL. You are talking about the $500 child tax credit, for example.

Mr. GREENSTEIN. Following the definition of people like June O'Neill at the Congressional Budget Office.

Senator KYL. Which includes the $500 child tax credit.

Mr. GREENSTEIN. Not as a business subsidy.

Senator KYL. No, but it is defined as a subsidy under that definition.

Mr. Norquist.

Mr. NORQUIST. This is an important debate that goes back a number of years. I remember in the late 1970's Teddy Kennedy started explaining that tax expenditures where over time the Government didn't take your money—that if a mugger didn't notice that you had $10 in your other pocket, he had just given you the $10 somehow when he took everything else. That is, again, the difference between people who stand in Washington and look at everybody out in the provinces as targets to be looted and people who live in the country who want to keep and maintain their own income.

The argument that if we don't take it from you, we gave it to you, is exactly what is wrong with this city and why there is such a huge distinction between the Government saying we are not going to take 80 percent of your income—that is not a gift of 80; that is a taking of 20. This is a procedural and a technical and a definitional debate, but it is a debate that comes up, constantly thrown up by those who argue against tax cuts and who think that tax increases and spending restraint are the same because they have the same effect on Washington, but not the same effect on people.

Mr. GREENSTEIN. I don't recognize that as a characterization of what I am saying at all.

Mr. NORQUIST. Of course, he doesn't.

Senator KYL. I appreciate the difference in viewpoint here.

I am going to conclude this hearing by reading something from the report that the Americans for Tax Reform put out which I think expresses the philosophy of many of the supporters of this amendment that raising taxes is not a way to ensure greater welfare. This goes directly—and this will be another disagreement that you and I have, Mr. Greenstein, that it is not necessary or even desirable to raise taxes to deal with the problems that we have; that, as a matter of fact, there is an optimum level of taxes which we have far exceeded and that at the optimum level we would have all been far better off.

So to your point that we are all going to have to suffer a bit more, there is probably nothing in your comments that I disagree with more than that. Americans don't have to suffer in order for us to get our budget deficit problem under control. As a matter of fact, we have a wonderful win/win opportunity here to both cut taxes, tax rates, and also achieve greater prosperity, including Government fiscal responsibility.

I am just going to read a bit from this report.

> Social welfare and economic growth would be maximized if Government revenue was one-quarter or less of the gross domestic product, in contrast with its present level of more than one-third of GDP. Beyond this point, any resources consumed by the Government impose more costs on the economy than benefits. Researchers have found that slow-downs in the rate of economic growth correlate with the growth in the Government's share of the gross national product. Estimates from this research show that Government maximizes economic growth when it is between 15 and 25 percent of GNP. Currently, total government taxation in the U.S. is 31 percent of GDP, while total government spending is 34 percent of GDP. For every dollar of Federal spending growth curtailed, the private sector will expand by $1.38 in the same year. Over 7 years, economic output would be $2.45 larger for each dollar of Federal spending restraint. If the tax burden had been at the optimal rate since World War II"—that is to say 25 percent instead of 31 or 34 percent—"economic growth would have averaged about 2 percent higher per year and the average American family would have about twice as much in real income as it actually has today.

Then skipping down to the final two sentences:

> If the U.S. had been spending at its optimal rate, between 15 and 25 percent of GNP, since World War II, real GNP in 1989 would have been $13.6 trillion instead of $6.2 trillion. The average American family would have twice as much real income as it has today.

I think this is an extraordinarily powerful argument for the proposition that the Government, the economy and American families, all three, would be better off with lower taxes, and that is one of the reasons why we want to make it harder to raise taxes through this constitutional amendment.

I very much appreciate the testimony of all four of the panelists. Mr. Greenstein, you were outnumbered here, but we appreciate your testimony, and we certainly appreciate the support of John Shadegg, one of the cosponsors of the amendment in the House. Good luck with your vote later on this afternoon.

Now, this hearing will recess, to be reconvened at 1 p.m. this afternoon.

[Whereupon, at 12:37 p.m., the hearing was adjourned to reconvene at 1 p.m., this same day.]

[The subcommittee reconvened at 1:24 p.m., Hon. Jon Kyl presiding.]

Senator KYL. The hearing of this subcommittee of the Senate Judiciary Committee will begin now with the statement of Senator Paul Coverdell of Georgia regarding the subject of Senate Joint Resolution 8, a proposed amendment to the Constitution to prohibit retroactive increases in taxes.

Senator Coverdell, if you are ready, proceed.

STATEMENT OF HON. PAUL D. COVERDELL, A U.S. SENATOR FROM THE STATE OF GEORGIA

Senator COVERDELL. Mr. Chairman, I appreciate the opportunity to appear before the committee, and the committee and its staff for facilitating this hearing. In advance, I want to thank the panelists that are prepared to testify on it; in particular, Joseph Schmitz of Patton Boggs; Dr. Roger Pilon, director of the Center for Constitutional Studies, of Cato; Ms. Joanne Dixon of Jirard, GA, a constituent and friend; and also Mortimer Caplin of Caplin and Drysdale, Washington, DC.

As the Chairman knows, we have just returned from a presentation on the floor of the U.S. Senate where for the better part of the morning we have been talking about the unbelievable accumulation of burden that has come to fall on the average working family in America and the average business in America. We had Senator after Senator talk in various forms about the scope of this burden.

I, Mr. Chairman, outlined an average family in my State which earns about $40,000. You can argue it a couple thousand one way or the other, but it is about $40,000 a year and they have two children and both spouses work. By the time they have paid their Federal taxes, their State taxes, their share of the national debt, interest payments that are pushed up, FICA, and their share of the regulatory burdens, it is about 50 percent. I think Thomas Jefferson would be rolling in his grave at the concept that 50 percent of the fruits of labor are being confiscated by one government or government policy, leaving the fundamental instrument of American society on which we depend so much to raise, house, feed, educate, provide for the health of our country so marginalized, so pushed to the wall, so barely able to carry out the duties upon which we depend so much as a Nation.

Mr. Chairman, in my judgment, the Government has had a more profound effect on the behavior of the American family than any other device or instrument, including Hollywood. I believe anything that could remove half the resources of a working family has to be pointed to as the No. 1 behavioral culprit. I think it has unalterably changed the way the family unit functions.

In the course of our discussion this morning, Mr. Chairman, we talked about the most recent addition to this burden, which was the tax increase imposed by the Clinton administration in August 1993. It is the largest in history, $250 billion-some-odd, but as I closed my remarks, I mentioned that we were having this hearing here today and that I thought the most egregious piece of that tax increase was the retroactive nature of it.

For the first time in history, Mr. Chairman, the tax increase which occurred in August 1993 reached all the way back to the first day of the current administration and then went beyond and

reached into a former administration. I mentioned that not even the Russian constitution now would allow that.

Mr. Chairman, it is just fundamentally and morally bankrupt, in my judgment, for an American family or an American business on the first day of the year not to understand what the rules of the road are. I think our Government, not only in the area of taxation, but throughout its behavior has increasingly and with more frequency been willing to change the rules of the road midstream, and in this case after the fact, leaving it most difficult for anyone to sensibly plan about this most important aspect of their lives; *i.e.*, their financial resources.

Now, throughout the course of this debate, we always hear considerable intellectualizing about the burden it would place on the Congress if it lost the flexibility to correct a mistake or to otherwise alter the behavior retroactively. To be candid, Mr. Chairman, I think the American family and citizen is a higher device to predict, their family, than the foibles of the Congress.

I think to argue that we must have this device and capacity to protect from error or misuse by citizens because we didn't see a loophole this egregious, that they have a higher standing than we, and that once we set the rules, their welfare should come first and ours second, not the reverse.

Mr. Chairman, I won't dwell on this long, but I would ask consent of the Chair that my formal remarks be put into the record and I will only close with one point, and that is that without citing all the reasons of *ex post facto* and other conditions in the Constitution, I believe the Forefathers never meant for there to be retroactive taxation. I know Jefferson would not have sanctioned it. They say *ex post facto* doesn't apply to civil circumstances, but, of course, if you don't pay your taxes, it is criminal.

I believe the Constitution is replete, at least in three separate occasions and instances, with direction that would suggest very strongly that the concept of retroactive behavior, particularly in the form of taxation, is wrong and should never have been a piece of our law, and that is what this constitutional amendment is meant to clarify, since we in our courts have seemed to develop so much difficulty in understanding what the direction of the document was.

I appreciate the opportunity to be with you today and I look forward to joining you, if I may, in listening to the testimony.

Senator KYL. Thank you. Senator Coverdell, may I ask you just a couple of questions?

Senator COVERDELL. You sure may.

Senator KYL. Were there not more than one feature of the 1993 tax code that were retroactive? There were 2 or 3 provisions that were made retroactive, were there not?

Senator COVERDELL. That is correct. I was referring, Mr. Chairman, to the general procedure. It affected several elements of the tax code, but, in essence, it was a process by which you reached back, as I said, even beyond the sitting administration or elected government into a former government.

Senator KYL. This amendment is about the simplest that I have ever seen. As a matter of fact, it is less than 2 lines long, "No Federal tax shall be imposed for the period before the date of enactment of the tax."

Senator COVERDELL. That is correct.

Senator KYL. It is hard to find fault with that, and I can't imagine that the Founding Fathers would have found fault with it, nor would they have had any trouble putting it in themselves if they could have foreseen what later Congresses have done.

I very much appreciate your statement, and please join me up here so that you may have an opportunity to visit with the remaining panel.

Senator COVERDELL. Mr. Chairman, I would be glad to do it. I see you are wearing a rather unique button relating to an earlier portion of the hearing, and I want to commend the Chairman for the extensive work in the arena of taxation and for the proposal you have put forth requiring an extra burden on the implementation of taxation.

I believe when you look at the types of procedures which require a higher burden, I can't think of one that is more appropriately placed on that pedestal, particularly in this day and time, than the taxing of the American citizen and family. I commend you for your work.

Senator KYL. Thank you, Senator Coverdell. Please join me here.

[The prepared statement of Senator Coverdell follows:]

PREPARED STATEMENT OF SENATOR PAUL D. COVERDELL

Mr. Chairman, I want to thank you and your staff for facilitating this hearing to discuss S.J. Res. 8, a proposed constitutional amendment to prohibit retroactive taxation by the federal government. I know how difficult it is to assemble this portion of the legislative process and how busy you have been with all the matters you are addressing in the 104th Congress.

I also want to thank the witnesses who have agreed to testify on S.J. Res. 8. They are "citizens at large" who have taken time from their routine and regular schedules and business to come and help our government work. I am particularly grateful for their presence.

I believe the American people in overwhelming numbers understand that retroactive taxation or, in other words, changing the rules midstream—after the fact—is wrong. I just do not believe you can intellectually defend the idea that a government such as ours or any government can arbitrarily step forward and change the rules under which our citizens have planned their lives. I do not believe you can find an audience in any area of the country, unless it is an intellectual exercise in an academic setting, that would find any agreement in such an idea.

When we put it in the context of a citizen, a family, or a business trying to put their lives in order, they have a right, in my judgement, to expect that what we have told them about the rules they are expected to follow and to expect we are not going to change them. I take the argument beyond taxation to many other congressional actions. With increasing frequency, we are destabilizing our communities, our families, and our businesses because of our tendency to change the process for which they are unable to prepare.

We all know the Constitution is the ultimate document governing us. Changes to it should not be attempted capriciously. I believe it already speaks to the question of retroactive taxation. There has been an erosion that has occurred within our judicial system. Over the years, it has diluted considerable constitutional language dealing with the question of retroactive taxation. In my judgement, there are at least three different statements made in the Constitution dealing with retroactive taxation. The drafters of the Constitution stated in Article I, Section 9, that no *ex post facto* law shall be passed.

It was not until the case of *Calder* v. *Bull* in 1798 that it was decided this provision was of limited application and only dealt with criminal law, not civil law. I am not sure that our forefathers really meant it in that way. I think *ex post facto* means *ex post facto*, and they were speaking to the idea that any law should not be changed after the fact.

Of the Supreme Court decision in *Calder*, Thomas Jefferson—I think we can consider him a preeminent authority—wrote, "ex post facto laws are against natural

right * * * [and] are equally unjust in civil as in criminal cases." I think our forefathers did not intend for this cleavage to occur.

The Founders provided a second protection against retroactive taxation in the Due Process Clause of the Fifth amendment to the Constitution. The clause prohibits the general government from taking property without providing due process of law. I consider the financial wealth of a family or a business as "property," and I do not believe, nor do I believe the Founders intended for due process to be set aside in the case of taxation. Common sense would suggest that it should not have been.

Most recently, in *U.S.* v. *Carlton,* the Supreme Court confirmed it will not prohibit the enactment of retroactive tax legislation under a due process analysis. So, again, we have an ongoing erosion by the Courts of the principle I believe is established firmly. This concept has been eroded to the point where it needs reinforcement, and clarity needs to be re-established in the Constitution.

A final Constitutional argument against last year's retroactive tax, not all of them but certainly last year's, is that it constituted a Bill of Attainder within the meaning of Article 1, Section 9. It is an act of the legislature punishing specific individuals. If you go back to the debate of the retroactive tax, it is absolutely without question that the law was driven at a specific sector of our society, that they could be set aside for unequal application of the law. I find to be inexcusable and inappropriate.

So what I hope to address here are two points. First, the Constitution already has embraced the idea of retroactive taxing. In three different provisions of the Constitution, it comes up to the idea that these changes retroactively are not right and should not occur in our country. Second, the other point I make, in light of the fact that it is already dealing with the subject, the question of whether or not this Constitutional amendment has standing is answered in the Constitution itself, because the Constitution already moves to the subject. It is not silent on the subject. It recognizes the importance of the subject and, in my judgement, tried to deal with it, not foreseeing the erosion that would occur because of our court system.

Again, Mr. Chairman, I want to thank you for calling the hearing and the opportunity to present testimony.

Senator KYL. We will next go to panel No. 5 of today's hearings—Joseph Schmitz, of Patton Boggs, a law firm in Washington, DC; Dr. Roger Pilon, director, Center for Constitutional Studies at the Cato Institute here in Washington, DC; Joanne Dixon, a homemaker from Jirard, GA; and Mortimer Caplin, of Caplin and Drysdale of Washington, DC. We welcome all of you to this hearing today. We are missing Mr. Caplin. Well, when Mortimer Caplin arrives, we will have him join us at the table.

Mr. Schmitz, would you like to begin and give your testimony, please, first?

PANEL CONSISTING OF JOSEPH E. SCHMITZ, PATTON BOGGS, WASHINGTON, DC; ROGER PILON, SENIOR FELLOW, AND DIRECTOR, CENTER FOR CONSTITUTIONAL STUDIES, CATO INSTITUTE, WASHINGTON, DC; MORTIMER CAPLIN, CAPLIN AND DRYSDALE, WASHINGTON, DC; AND JOANNE DIXON, RETIRED FARMER, JIRARD, GA

STATEMENT OF JOSEPH E. SCHMITZ

Mr. SCHMITZ. Thank you, Senator Kyl. First of all, I would like to thank Chairman Brown for inviting me to testify today.

Three years ago, I represented the Washington Legal Foundation, Chairman Hatch, Speaker Gingrich, and 40 other Members of Congress in an amicus curiae brief in the retroactive tax case called *United States* v. *Carlton.* For those who suggest today that it would not be wise to amend the Constitution or otherwise to adopt legislation that would prohibit retroactive application of a tax increase, my response is not only that our Founding Fathers would favor such a prohibition, but that they included such a pro-

hibition in the *Ex Post Facto* and the Due Process Clauses of the Constitution.

I dare say the most revolutionary of our Founding Fathers might have even tried to lynch anyone for suggesting the need for debate over the issue of retroactive taxation. The Boston Tea Party, don't forget, was about taxation. Of course, before penalizing or taxing anyone for suggesting such a debate, the revolutionaries who drafted our Constitution and Bill of Rights would have provided the guilty party at least advanced notice and an opportunity for a hearing.

The Supreme Court in its 1994 *Carlton* decision ignores both the *ex post facto* and the procedural due process arguments raised by 42 Members of Congress in their amicus brief, instead dwelling on a substantive due process claim which the lower court in California had actually sustained. During oral argument, when asked by Justice Stevens whether his client's due process claim was procedural or substantive, counsel for *Carlton* responded, "To be perfectly honest, Your Honor, I have never been able to figure out the difference." The Supreme Court ruled against *Carlton* 9 to 0.

While rummaging through a pre-New Deal legal lexicon earlier this month, I discovered what some might regard as a novel definition of "due process of law," as explained by the U.S. Supreme Court in 1913. The case arose out of a retroactive change in the amount of time required in Puerto Rico before a fraudulent occupier of private property could claim title to the property he was occupying.

The Supreme Court in that case explained, "Whatever else may be uncertain about the definition of the term 'due process of law,' all authorities agree that it inhibits taking of one man's property and giving it to another contrary to settled usages and modes of procedure and without notice or an opportunity for a hearing."

By the way, the Supreme Court decided *Ochoa,* which is the name of this case, 4 months after ratification of the Sixteenth Amendment which authorized Congress, "to lay and collect taxes on incomes without apportionment among the States."

On tax day 1996, 83 years after the States ratified the Sixteenth Amendment, and after the Supreme Court decided the *Ochoa* case, whatever else may be uncertain about the definition of the term "taxation," all authorities would have to admit that Federal taxation today involves wealth transfer. Simply stated, modern Federal taxation involves taking money from certain citizens and giving that money to others. In 1913, the Supreme Court concluded that engaging in that process retroactively violates "fundamental principles known wherever the American flag flies." Today, these fundamental principles are still at the heart of the debate over retroactive taxation.

Before discussing how the Supreme Court addressed retroactivity in *Ochoa* and then retroactive taxation in *Carlton*, I would like to delve a bit deeper into the history of due process to a time when a certain Roman emperor was having problems with, among other things, raising revenues.

Two thousand years ago, Emperor Caligula was having difficulty balancing the budget of the Roman Empire. When his coffers were nearly empty, Caligula would raise additional revenues by writing

new laws in small characters and posting them upon high pillars. When the wealthy citizens of Rome failed to heed these new laws, Caligula reportedly imprisoned them, killed them and, of course, confiscated their wealth. By the way, Caligula was assassinated in the year 41 A.D., in his fourth year as emperor and at the ripe old age of 29.

Shortly before the American Revolution, Sir William Blackstone published in England a comprehensive treatise on English law known as *Blackstone's Commentaries,* in which Blackstone cites Caligula's method of raising revenues as an example of how not to notify the people of a new law, such notification, according to Blackstone, being an essential element of any new law.

Immediately after disparaging Caligula for ensnaring his own people through illegible laws, Blackstone writes, "There is still a more unreasonable method of notification than this, which is called making the laws *ex post facto.*" All laws, according to Blackstone, "should be therefore made to commence in futuro and be notified before their commencement."

The drafters of the Constitution apparently read Blackstone well and were not fans of Caligula. They included in Article I of the Constitution two explicit prohibitions against *ex post facto* laws, one for Congress and one for the States. Whatever else may be uncertain today about the drafters' definition of the term "*ex post facto*," we do know that retroactive legislation generally was abhorred not only by Blackstone, but by most, if not all, English-speaking proponents of the rule of law in the 18th century.

For instance, James Iredell, later a Justice of the U.S. Supreme Court, argued in 1787 during the constitutional debates that, "*Ex post facto* laws have been the instrument of some of the grossest acts of tyranny that were ever exercised."

In 1798, however, the Supreme Court construed the constitutional prohibitions against State, as opposed to Federal *ex post facto* laws as applying only to criminal type laws. That decision, *Calder* v. *Bull,* involved a probate dispute in Connecticut and turned on the historical fact that the Connecticut Legislature, like parliament and unlike Congress, was authorized to reverse judicial decisions.

Almost 200 years later, the Federal *Ex Post Facto* Clause has never been independently construed by the Supreme Court or by any other court, to my knowledge. The Federal *Ex Post Facto* Clause has always been lumped together with the State prohibition and accordingly limited to criminal laws in accordance with the Supreme Court's 1798 decision regarding Connecticut probate law.

But failure to pay Federal taxes in the 20th century, as Senator Coverdell aptly pointed out, is a crime. Section 7203 of the Internal Revenue Code, for instance, makes it a misdemeanor to willfully fail to pay a Federal tax, the penalty for which is up to $25,000 for individuals, $100,000 for corporations, and/or imprisonment for up to a year. I dare say had I or anyone else willfully failed to pay retroactively increased income taxes in 1993, I and whoever else might have done that could have gone to prison for a year. Accordingly, the constitutional prohibition against *ex post facto* laws, even if restricted to criminal type laws, should apply to retroactive Federal tax laws.

I see my red light is on.

Senator KYL. Yes. We have a 7-minute rule today and if you could please try to summarize, of course, all of your statement will be included in the record and we will have some questions which might draw out additional aspects of your testimony. Thank you.

Mr. SCHMITZ. Let me just try to summarize quickly. *Carlton*, the Supreme Court's case in 1994, completely ignored both the *ex post facto* and the procedural due process arguments raised by the 42 Members of Congress. They only addressed the substantive due process claim raised by *Carlton*. So, theoretically, another case might actually come out differently and restrict Congress' power. But *Carlton*, in my opinion, was a democratic call to arms. They could have addressed these issues. Instead, what they did, in effect, was say this issue is really too hot for us.

So the critical question which remains for this committee and ultimately for the American people—well, there are two questions; No. 1, whether this Congress is willing to do a little bit better than Caligula and restrain itself from enacting retroactive tax laws, and No. 2, if so, how should such restraint be crafted. Enactment and ratification of Senator Coverdell's proposed amendment would resolve these questions once and for all, thus ensuring Emperor Caligula's singular place in history as the paradigm of how not to raise revenues.

Senator KYL. Thank you very much.

[The prepared statement of Mr. Schmitz follows:]

PREPARED STATEMENT OF JOSEPH E. SCHMITZ

ARTICLE—

"Section 1. No Federal tax shall be imposed for the period before the date of enactment of the tax."

"Section 2. This article shall take effect the date of its ratification."

First of all, I would like to thank Chairman Brown for inviting me to testify today. My name is Joseph Schmitz. I am a partner at the law firm of Patton Boggs. I am also an Adjunct Professor of Law at Georgetown University Law Center, where I teach an advanced Constitutional Law seminar.

Three years ago I represented the Washington Legal Foundation, Chairman Hatch, Speaker Gingrich, and 40 other members of Congress in an *amici curiae* brief to the United States Supreme Court in the retroactive federal tax case, *United States* v. *Carlton.*

Retroactive taxation is already prohibited by at least two constitutional provisions. The first is the federal *ex post facto* clause, which states: "No * * * ex post facto law shall be passed." (Art. I, § 9) The second is the federal due process clause, which states: "No person shall be * * * deprived of life, liberty, or property, without due process of law." (Amend. V) Regarding ex post facto, if a citizen does not pay a retroactive tax, he can be criminally prosecuted. That sounds like an *ex post facto* law to me. Regarding due process, retroactively taking money from private citizen and businesses is fundamentally antithetical to *procedural* due process, which includes among its essential attributes "prescription" and notice. The Supreme Court avoided both these issues in deciding *Carlton,* instead dwelling on a *substantive* due process claim, which the lower court in California had actually sustained. During oral arguments before the Supreme Court, when asked by Justice Stevens whether his due process claim was procedural or substantive, Counsel for Carlton responded, "To be perfectly honest, your honor, I have never been able to tell the difference." The Supreme Court ruled against Carlton 9–0.

While rummaging through a pre-New Deal legal dictionary earlier this month, I discovered a novel definition of "due process of law": "While the exact definition of 'due process of law' may be uncertain, it is certain that it inhibits the taking of one man's property and giving it to another, contrary to settled usages and modes of procedure, and without notice or an opportunity to be heard." [citing *Ochoa* v. *Hernandez,* 230 U.S. 139, 140 (1913)] Before discussing how the Supreme Court ad-

dressed retroactive taxation in Carlton, I would like to delve a bit deeper into the history of due process, to a time when a certain roman emperor was having problems with, among other things, raising revenues.

Two thousand years ago, Emperor Caligula reportedly had difficulty balancing the budget of the Roman Empire. When his coffers were nearly empty, Caligula would raise additional revenues by writing new laws in small characters and posting them upon high pillars. When wealthy citizens of Rome failed to heed these laws, Caligula reportedly imprisoned them, killed them, and, of course, confiscated their wealth. By the way, Caligula was assassinated in the year 41 A.D., in his fourth year as Emperor and at the ripe old age of 29.

Shortly before the American Revolution, Sir William Blackstone published in England a comprehensive treatise on English law known as Blackstone's *Commentaries on the Laws of England.* In his *Commentaries*, Blackstone cites Caligula's method of raising revenues as an example of how *not* to notify the people of a new law—such notification, according to Blackstone, being an essential element of any civil law. Immediately after disparaging Caligula for "ensnaring" his own people through illegible laws, Blackstone writes: "There is still a more unreasonable method [of notification] than this, which is called making of laws *ex post facto.*" "All laws," according to Blackstone, "should be therefore made to commence in *futuro*, and be notified before their commencement."

The drafters of the Constitution apparently read Blackstone well—and were no fans of Caligula. They included in Article I of the Constitution two explicit prohibitions against *ex post facto* laws, one for Congress and one for the States. Despite the clarity of Blackstone's *Commentaries,* most modern scholars agree that it is not clear what the term *"ex post facto"* was understood by the drafters to entail.

We do know, however, that retroactive legislation generally was abhorred not only by Sir William Blackstone, but by most if not all other prominent English-speaking proponents of the rule of law in the Eighteenth Century. For instance, James Iredell (later a Justice of the United States Supreme Court Iredell) argued during the constitutional debates in 1787 that "*Ex post facto* laws * * * have been the instrument of some of the grossest acts of tyranny that were ever exercised."

In 1798, however, the Supreme Court construed the constitutional prohibition against state—as opposed to federal—*ex post facto* laws as applying only to criminal-type laws. That decision, involving a probate dispute in Connecticut, turned on the historical fact that the Connecticut legislature—like Parliament and unlike Congress—was authorized to reverse judicial decisions. [*See Calder* v. *Bull,* 3 U.S. (3 Dall.) 386 (1798).] Almost two hundred years later, the federal *ex post facto* clause has never been independently construed by the Supreme Court—or by any other court to my knowledge. The federal *ex post facto* clause has always been lumped together with the state prohibition, and accordingly limited to criminal laws in accordance with the U.S. Supreme Court's 1798 decision regarding Connecticut.

But failure to pay federal taxes in the Twentieth Century is a crime. Section 7203 of the Internal Revenue Code, for instance, makes it a misdemeanor willfully to fail to pay a federal tax, the penalty for which is up to $25,000 for individuals ($100,000 for corporations) and/or imprisonment up to one year. And I dare say, had I willfully failed to pay my retroactively increased income taxes for 1993, I could have gone to prison for a year.

The Supreme Court's 1991 decision in *Cheek* v. *United States,* 498 U.S. 192 (1991), illustrates that there is no "bright line" between civil and criminal tax cases, and that one who protests retroactive taxes by not paying them is subject to criminal penalties. Accordingly, the constitutional prohibition against *ex post facto* laws, even if restricted to criminal-type laws, should apply to retroactive federal tax laws.

The Supreme Court's decision in *Carlton,* however, suggests that the Court is unwilling to impose any meaningful restraints on Congress, ability to enact retroactive tax increases. *Carlton* was a constitutional disappointment because, among other reasons, the Court completely ignored a compelling *ex post facto* argument raised by 42 Members of Congress. The court in *Carlton* addressed only the substantive due process challenge raised by Mr. Carlton in that case. Theoretically, therefore, another retroactive tax case might come up to the Court under a different provision of the Constitution, perhaps even under the federal *ex post facto* clause, which, as I have said, has never been independently and definitively adjudicated by the Supreme Court.

Carlton was also a democratic call to arms because by ignoring the *ex post factor* argument of 42 Members of Congress, the Justices of the United States Supreme Court, in three separate opinions, in effect, said: This issue is too hot for us to handle—it's up to the political branches or to the people to impose any restraints on retroactive federal taxes.

The critical questions which remain for this Committee and ultimately for the American people are: (1) whether this Congress is willing to do better than Caligula and restrain itself from enacting retroactive tax laws; and, if so, (2) how should such restraint best be formalized? Senator Coverdell's proposed constitutional amendment is an excellent vehicle for addressing both questions.

Enactment of this proposed constitutional amendment, with ratification by the States, would resolve the issue once and for all; thus ensuring Caligula's singular place in history as the paradigm of how not to raise revenues.

Senator KYL. Dr. Pilon.

STATEMENT OF ROGER PILON

Mr. PILON. Thank you very much, Senator Kyl, and I want to thank Senator Brown and Senator Coverdell for their kind invitations to be here to testify today. I would ask that my prepared statement be included in the record. I will just summarize a few points from it here this afternoon.

In a way, this issue that is before us, retroactive taxation, should never be before us, as Mr. Schmitz has just demonstrated convincingly, to my judgment. The Constitution addresses this issue plainly. The courts have ignored or rewritten the Constitution and the relevant provisions. That is why we are here, and now it falls to the Congress to take up the slack and see to it that this issue of retroactive taxation is buried once and for all and I urge you very much to do that and will do so at the conclusion of my remarks here.

The issue of retroactive taxation is in many ways so elementary that it is almost embarrassing to have to speak to it. It is the kind of thing that any child understands on the playground under the simple admonition you don't change the rules after the game has begun. In fact, this is even worse than changing the rules after the game has begun and changing the rules in the middle of the game. You are actually changing the rules back to the beginning of the game, and we all understand that so elementary a move as that is just simply—you wouldn't get away with it in a Monopoly game, you wouldn't get away with it in a basketball game. You shouldn't get away with it in the Congress of the United States, but you do. You do because the courts have not been doing their job.

Now, I am not a tax lawyer or an expert on taxation. My field is the philosophy of law, so I am not burdened by the details of tax law. I can step back and look at some of the larger issues, and that is what I want to do here and address some of these deeper issues, some of which Senator Coverdell touched upon in his opening remarks, because the issues take us to some very fundamental questions of political philosophy and, in particular, to the foundations of political obligation, including the obligation to pay taxes.

If this Nation is founded indeed upon the idea of individual liberty and individual autonomy, then there are two considerations at common law that we refer to as sources of obligation. They are, on the one hand, consent, and on the other hand a breach of some natural duty. In other words, we are not rooted as a Nation in some organic conception of political obligation of the kind that President Clinton invoked in his inaugural address by implication when he said we are all in this together. We are not all in this together. We are individuals and we come together only for those issues that are properly in the public domain, the rest being in the private domain,

as the tenth amendment and other parts of the Constitution make explicitly clear.

If we are rooted in consent out of a deep respect for individual autonomy, then the question arises how is it that we have gotten where we are today where constitutional restraints that are meant to secure that autonomy have been so atrophied over the course especially of the 20th century. They have been abandoned by the courts at the urging of the political branches and been replaced by the kinds of benefits and burdens talk that we find in Justice Stone's opinion in *Welch* v. *Henry,* which is the locus classicus in 1938 of the modern doctrine that justifies or purports to justify retroactive taxation.

The result of that is to leave individuals and firms out of court. I mean, they essentially have no longer any legal appeal. They have only a political appeal in these matters and when that is the case, when they have no legal remedy for those who are unjustly burdened as they are taxed to provide benefits for those who are unjustly enriched, we have the modern redistributive state. We have substantive and procedural unfairness in this.

Substantively, you have great partiality and inequality. Procedurally, pertaining to questions like retroactivity, you have due process effectively denied. In both cases, the victims are out of court. Ironically, therefore, we have to turn to the political branches for what should be addressed by the judicial branch. When judicial review is essentially unavailable, tyranny is invited. It is just that simple. What is retroactivity, the changing of the rules after the fact, if not the very essence of tyranny?

But look at some of the substantive and procedural issues at stake. Substantively, if individual autonomy is indeed the premise, then government should have only that power that is necessary to secure our autonomy. In that context, the power to tax is an instrumental power, but it must be exercised consistent with the basic premise from which it flows. Hence, it must be limited and equal.

The more government expands, the more taxation does, and the less consent for that taxation can be found, which is presumably the bedrock principle of this Nation. Look at it procedurally. Retroactivity raises conspicuously the issue of notice. What you have got is you have no notice and that relates to fairness. How can people arrange their affairs if the rules for doing so are going to be changed retroactively? You simply can't penalize people for behavior they had no reason to believe was subject to penalty. That is, again, the essential principle that is involved in retroactive taxation. So the *Ex Post Facto* Clause, as Mr. Schmitz has said, as well as the Due Process Clause should more than address this.

Let me say, finally, a few things about a couple of the practical issues that arose last time this committee held hearings on this issue and should be addressed, it seems to me. Some have argued, for example, that by focusing on date of enactment, as this amendment does, that we risk ignoring those adversely affected by legislation that is nominally prospective because all changes will affect somebody who has arranged their affairs according to them. Even you make those changes prospective, you may have diminution in value of assets, and so on and so forth.

Well, the argument is perfectly generalizable. Every time you have a change, there are retroactive effects. So, in effect, the argument argues too much. That really is counsel for doing nothing at all about anything at all. Of course, that is hardly a position we want to bootstrap ourselves into in the name of arguing against an amendment that would prohibit retroactivity. What you need to do, rather, is recognize that this is indeed the case and address those particular cases on a case-by-case basis, maybe with some provisions for compensation among those who are adversely affected by that.

Now, the second objection that is sometimes raised is one that argues from a perception of fairness which is lost when Congress makes mistakes or individuals find loopholes in tax law. Well, there it seems to me Senator Coverdell addressed that very briefly in his opening remarks, and that is that the fairness may require retroactive correction, so the argument goes. In other words, the opponents argue that substantive unfairness should trump procedural unfairness. That, of course, taken to its logical conclusion, is a prescription for anarchy.

In addition to that, when Congress tries to correct its mistakes by shifting responsibility from itself to the victim of its mistakes, you have compounded the error, and that is indeed exactly what happened in the *Carlton* case that the Court decided in 1994 when the executor of the estate, who was duty-bound to maximize the estate, was penalized for exercising the diligence he is required to exercise as executor of the estate. I mean, this is a fine state of affairs we have put the executor into. He is damned if he does, he is damned if he doesn't. Yet, that is exactly what you get into with the kind of retroactivity that we see too often coming out of the Congress.

So when we recognize, let me say in conclusion, that the substantive unfairness is usually widely spread and small when you are dealing with mistakes that Congress has made, whereas the procedural unfairness of retroactive taxation is usually concentrated and large in any given case, it seems to me the arguments for retroactivity are overwhelming and beyond doubt, and I would urge you therefore to go forward with this because it is the kind of thing that rings true with the American people and I think you would find wide receptivity and I think you would find this amendment sailing through three-quarters of the legislatures it must sail through.

Thank you.

Senator KYL. Thank you, Dr. Pilon.

[The prepared statement of Mr. Pilon follows:]

PREPARED STATEMENT OF ROGER PILON

Mr. Chairman, distinguished members of the subcommittee, My name is Roger Pilon. I am a senior fellow at the Cato Institute and the director of Cato's Center for Constitutional Studies.

I want to begin by thanking Senators Brown and Coverdell for inviting me to speak before this subcommittee in support of S.J. Res. 8, proposing an amendment to the Constitution to prohibit retroactive increases in taxes.

When hearings on retroactive taxation were proposed in the Senate in October of 1993, following the retroactive tax increase that President Clinton signed into law that year, Senator Richard Shelby, then of the President's party, asked rhetorically of the Senate President, "Why do we need hearings to consider the retroactivity of

taxes * * * when we basically and the American people believe it is wrong?" In thus representing the beliefs of the American people, Senator Shelby got it exactly right, of course. At bottom, in fact, the issue of retroactive taxation is no more complicated than the sports analogy every child learns on the playground—it's wrong to change the rules after the game begins.

Unfortunately, that simple rule, to say nothing of the beliefs of the American people, has been little regarded over the course of this century as legislatures have grown increasingly fond of their powers to tax, including their power to tax retroactively. And the courts, for their part, have grown increasingly deferential to those legislatures. Given those facts, extraordinary measures—and a constitutional amendment is extraordinary—are in order.

Unlike my fellow panelists today, Mr. Chairman, I am not a tax lawyer or an expert on taxation. I don't even do my own taxes. Rather, my field is the philosophy of law, which means that I try, if at all possible, not to look too closely at the trees so that I can keep my eye on the forest.

Unfortunately, tax law today is almost all trees and no forest. Despite occasional efforts at "simplification," our tax law is the chaotic product of all but unbridled political will, nominally enacted to raise revenue, but interlarded throughout with public policy—with social policy undertaken through the tax code. (Those on my side of the political divide who oppose government planning through redistribution and regulation, but support every "tax break" that comes along, are too often prone to forget that "tax policy," thus understood, is just a poor man's (rich man's?) way to try to manage an economy.)

When I say that our tax law today is a product of all but unbridled political will, I mean, among other things, that in perhaps no other area of our law are the courts so deferential to the political branches. Well before the Supreme Court set forth its general theory of deference in 1938 in famous footnote four of *Carolene Products*[1]—wherein the Court distinguished two kinds of rights, fundamental and nonfundamental, and two levels of judicial review, strict and minimal, relegating "ordinary commercial transactions" to the latter category—the Court was deferring to the political branches on issues of taxation.

Yet it was Justice Stone, the same Justice Stone who wrote the opinion in *Carolene Products*, who that very year set forth what, for lack of a better argument, has come to be the modern rationale for taxation generally and retroactive taxation in particular:

> Taxation is neither a penalty imposed on the taxpayer nor a liability which he assumes by contract. It is but a way of apportioning the cost of government among those who in some measure are privileged to enjoy its benefits and must bear its burdens. Since no citizen enjoys immunity from that burden, its retroactive imposition does not necessarily infringe due process. * * *[2]

Indeed, notwithstanding the classic *non sequitur* in Justice Stone's final sentence, the Court without a blush set forth that very rationale less than two years ago when it upheld the retroactive imposition of an estate tax change in the *Carlton* case.[3]

No one could disagree, of course, that taxation is "a way of apportioning the cost of government." But the contention that those who enjoy government's benefits "must bear its burdens"—an argument as old as Plato's *Crito*—is as circular as it is destructive of our founding principles.

At common law, one could incur obligations, or burdens toward others, in only two basic ways: either by contract, through consent, or by breach of some natural duty, leading to a penalty through the law of torts—the exact rationales Justice Stone rejected out of hand. Yet the first of those rationales, consent, constitutes the very foundation of our political order—and, by implication, of our tax policy. As both the Declaration of Independence and the Constitution make clear, we constituted ourselves politically through consent. In so doing we explicitly rejected older organic conceptions of political obligation, with their benefits-and-burdens rationales, because our fundamental moral principle was individual autonomy. Individuals are and ought to be free, we declared, except insofar as they bind themselves through their promises or their torts. (Doubtless, one often ought to reciprocate for the gratuitous receipt of benefits, but that is not the stuff of moral or legal obligation.)

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[1] *United States* v. *Carolene Products Co.*, 303 U.S. 144 (1938). I have criticized that opinion in Pilon, "On the Foundations of Economic Liberty," 38 *The Freeman* 338 (1988).

[2] *Welch* v. *Henry*, 305 U.S. 134, 146-47 (1938).

[3] *United States* v. *Carlton*, 513 U.S.—(1994); 62 U.S.L.W. 4472, 4475 (U.S. June 13, 1994).

In recognizing consent as our bedrock political principle, however, we also recognized the practical limits of that rationale, especially as it operates over succeeding generations. Thus, as a further protection for individual autonomy—beyond that afforded by original ratification and subsequent periodic elections—we limited the scope of government. Indeed, the Constitution is properly read not simply as instituting political power through the consent of the founding generation but as severely restraining power as well—for the benefit of succeeding generations—through such familiar devices as the separation and division of powers, the enumeration of federal powers, the addition of a bill of rights, and, of particular importance for the issue at hand, the institution of judicial review.[4] Notwithstanding those further restraints, however, consent remained the basic rationale for political obligation, even as its practical limits were recognized.

This inherent tension between our avowed foundation in consent—best captured, perhaps, by the colonial cry, "No taxation without representation"—and its practical limits is exacerbated, of course, as the scope of government grows, as the claim that "we" consented to, say, all the government we're getting today becomes increasingly implausible. Faced with that implausibility, one either abandons the consent rationale, as Justice Stone did, or complains about growing illegitimacy, as many of us have been doing since modern expansive government began during the Progressive Era. To abandon the consent rationale, however, is to abandon the premise of individual autonomy on which it rests, and to bring us face-to-face with our first president's insight that government is neither reason nor eloquence but force—and its corollary, the more government, the more force in our lives.

Those are the brute moral facts of the modern political dilemma, which no talk of "democratic decisionmaking," much less benefits and burdens, can argue away. And nowhere are those facts more starkly borne out, perhaps, than in the realm of taxation, where Justice Stone's vaunted rationale translates all too quickly into benefits for some and burdens for others—hardly a result to command universal consent. But the reality of the matter is starker still, for rarely if ever is that result underwritten by majoritarian consent either—quite apart from whether majority rule can justify anything. Rather, as the Public Choice school of political economy has repeatedly demonstrated, modern tax policy constitutes perhaps the paradigmatic example of special-interest politics at work. That politics is so far from being rooted in consent as to make a mockery of our founding doctrine.

In resorting to an older organic rationale, then, the benefits-and-burdens people have ignored both our origins in consent and the constitutional barriers we erected in light of the practical limits of consent, both of which are rooted in our concern for individual autonomy. Thus disparaging individual autonomy, they cling instead to visions of grand democratic undertakings, as stated succinctly by President Clinton in his inaugural address: "We're all in this together."

The problems with that view are many, of course, but chief among them are two: (a) we are not all in this together—many of us never wanted in, want out now, want simply to plan and live our own lives, not have them planned for us through the taxing and spending powers of Congress; and (b) the effort to force us to be part of the common undertaking, despite the lack of consent, is fraught with constitutional peril, both substantive and procedural. To put the point otherwise, America was not constituted as a parliamentary democracy, our fate to be determined in principle by transient majorities, in practice by those with access to political power. We are, rather, a constitutional republic, where political power is bounded by a constitutional rule of law.

Yet it is precisely that rule of law that the benefits-and-burdens Court, a Court that has lost touch with our founding principles,[5] has refused to secure. The practical effect of the Court's deference is to leave the determination and distribution of benefits and burdens to the political branches—which means, again, to the special interests that have learned so well how to work the system. What that means in turn is that the individual or firm that is adversely affected by the outcome of the process in which it is thus forced to participate is essentially out of court, with no legal remedy.

On the substantive side, great partiality and inequality are too often the result—with "soak the rich" being only one variation of this. On the procedural side, where the retroactivity issue arises here too the adversely affected individual or firm is, in effect, out of court. When judicial review is essentially unavailable, tyranny is in-

[4] I have discussed those issues more fully in Pilon, "A Government of Limited Powers," ch. 3, *Cato Handbook for Congress* 17–34 (1995).

[5] I discuss this point more fully in Pilon, "A Court Without a Compass," 40 *New York Law Review* (1996) (forthcoming) (symposium on James F. Simon's *The Center Holds: The Power Struggle Inside the Rehnquist Court* (1995)).

vited. And what is retroactivity—changing the rules after the fact—if not the very essence of tyranny?

Because the Supreme Court has demonstrated over the years—and as recently as two years ago—that it will not address this tyranny by applying the constitutional remedies that are readily available, we must turn, ironically, to the political branches to protect us from the political branches, which is what the amendment before us is aimed at doing. Because I am, with the Founders, of the individual autonomy school, not the grand undertaking school, I support the amendment. To elaborate further upon my reasons, however, and to address some of the concerns of the other side, I believe it would be useful to at least sketch both the substantive and the procedural issues at stake, first with respect to taxation generally, then with respect to retroactivity in particular.

If individual autonomy is indeed our basic moral principle, then government should have available to it only those powers that are consistent with securing that end. (Today, of course, thanks to the demise of the enumerated powers doctrine and all but boundless interpretations of the Constitution's General Welfare and Commerce Clauses, the powers of the federal government are restrained for the most part only by varying interpretations of the document's amendments.[6]) In that context, the power to tax is instrumental: it is a means to the exercise of other powers, themselves aimed at securing liberty. Like those other powers, however, the power to tax must be exercised consistent with liberty.

We come, then, to the nub of the substantive matter. For if the power to tax must be exercised consistent with liberty, it can be thus exercised only insofar as it is consented to. (The colonists had it right.) But universal consent, again, is impossible to obtain practically, which means that we have to look for conditions that at least move us in that direction. Two such conditions suggest themselves: (a) limited taxation, such that most people believe that the small cost of government is worth the limited benefits government provides; and (b) equal taxation, to ensure fairness among individuals, with no one burdened more than anyone else.

With respect to the first of those conditions, clearly, the more government decides to do, the more it needs to tax; and the more it taxes, the less universal the consent will be. The tax revolt of the past several years in this country is about nothing if not that. That revolt will dissipate only when our governments return to their natural and original limits--as governments around the world, which have much further to go, are today beginning to do.

With respect to the second condition, the basic question could not be simpler: Why should one person be burdened more than another by the costs of public services? Apart from user fees, which address the benefits-and-burdens question on an individualized basis, there is simply no credible reason why ability to pay should play any role at all in determining the distribution of the burden, not if we take equality seriously.

The impetus for unequal treatment in the area of taxation—which we would countenance for not even a moment with other burdens, such as criminal penalties or military service—was especially intense during the Progressive Era, of course, an era noted for its zeal for collective undertakings "in the public interest" and its animus toward trusts and other sources of wealth. How else to explain the ratification, however uncertain that process, of an income tax amendment, no less, except that it was to be limited to a rate of 1 or 2 percent and applied only against the wealthy. But that historical impetus in no way justifies our using some for the benefit of others, which is precisely what unequal taxation amounts to.

Notwithstanding the Constitution's enumerated-powers and equal-protection guarantees, both of which could have been read by the Court as restraining the political forces that have produced the expansive and unequal tax arrangements we have today, the Court has declined to secure those substantive protections. But the Court has done no better with procedural protections, not even in the case of retroactive taxation, which is so glaring an abuse of legal process as to require little argument against it.

Among the arguments against retroactivity is the argument from notice. Tax law today is so far removed from natural law and natural law principles that no one could possibly know its content from reason alone—as one can know, say, that murder, rape, and robbery are wrong. Those subject to taxation, therefore, must be given notice of the particulars so that they can adjust their behavior accordingly.

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[6] I have discussed that history and its implications in Pilon, "Freedom, Responsibility, and the Constitution: On Recovering Our Founding Principles," 68 *Notre Dame Law Review* 507 (1993); and Pilon, "On the Folly and Illegitimacy of Industrial Policy," *Stanford Law & Policy Review* 103 (1993).

To do otherwise is to penalize people for behavior they could not possibly have known was subject to penalty. It is the very antithesis of the rule of law.

As was argued by my fellow panelist, Mr. Schmitz, when we last testified before this subcommittee on this issue in August of 1994, the Constitution's *ex post facto* clauses, properly interpreted and applied, should alone suffice to preclude this kind of abuse of legal process—broadly understood to include the legislative process as it affects individuals not directly a part of it. But the Due Process of Law Clause, under which the 1994 *Carlton* case was decided, should suffice as well. Here again, however, one despairs of finding relief from a Court whose reasoning throughout is simply conclusory. When retroactivity longer than a year preceding the legislative session in which it is enacted raises "serious constitutional questions" whereas retroactivity short of that does not[7]—a line between unconstitutional and constitutional that is nowhere remotely to be found in the document—we know we have to look somewhere other than to the Court for the protection of our liberties.

Now it is argued by some who oppose this amendment, such as Mr. Ronald A. Pearlman, who appeared with Mr. Schmitz and me on that 1994 panel, that by focusing on "'date of enactment,' * * * we risk ignoring a large group of taxpayers that will be adversely affected by legislation that is nominally prospective,"[8] for even prospective changes often have retroactive implications. Indeed, Mr. Pearlman continues, "[e]very time Congress changes tax rates, whether the rates are increased or decreased, certain previously committed economic activity is affected."[9] Just so. Far from being an argument against this amendment, however, that observation makes the case for circumspection generally, especially since so much economic activity today is tax driven.

But the problem to which Mr. Pearlman points is broader than he seems to have appreciated, and perfectly generalizable. In a nutshell, through our tax law today, and not our tax law alone, we have brought about and encouraged a set of public and private arrangements upon which people have come to rely and a set of expectations about the future—not unlike those in the more socialized countries, except in degree. What we face, accordingly, is the same problem that people in the socialist countries are facing as they try to undo the past, namely, that it is terribly easy to get into those arrangements but terribly difficult, because people have come to rely upon them, to get out. We have created, in short, our own retroactivity problem.

None of that argues against this amendment, however, for if taxation is seen not as a zero-sum game—where one person's tax abatement is another person's tax assessment, a view Mr. Pearlman suggests when he speaks of threats "to the income tax base"[10]—but as a method of raising revenue fairly, then the question is not how we preserve (or enlarge) the current tax flow but how we move toward limited and equal taxation, mindful that some have arranged their affairs, in light of current law, in such a way as to be disadvantaged, at least for a time, by any such move.

Let me suggest that we address that problem, as best we can, on a case-by-case basis, even as we move in the right direction more generally. Since it was we who originally created the incentives that have encouraged people to make investments that may now be sunk when we change the rules again, albeit in the right direction, we should bear the costs of our change in direction rather than let those costs fall on innocent individuals. This is not like compensating slaveholders after Emancipation—people who relied on positive law that, by natural law principles, was conspicuously wrong from the start. Rather, tax law today is, again, sufficiently removed from natural law to make it all but arbitrary; yet it is a body of law upon which prudent people do and must rely as they arrange their affairs. Given that, we need to address the retroactivity costs to individuals and firms that arise even in the case of nominally prospective changes.

But if the difficulty today of discovering purely prospective tax law changes does not militate against this amendment, neither do the arguments from fairness that Mr. Pearlman has adduced. Thus he speaks of "the perception of fairness" as

> one of the principal reasons that President Reagan supported changes in the tax law that were designed to limit abusive tax shelters in 1984 and, thereafter, as part of the Tax Reform Act of 1986. * * *
>
> Fairness also must influence the adoption of effective dates for tax legislation. * * * Fairness requires, on occasion, explicitly retroactive tax legislation, such as in the case of the 1984 tax-exempt entity leasing provisions. I am confident that the American people would not want perceived abusers to be able to

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[7] *Carlton*, 62 U.S.L.W. 4472, at 4476 (Justice O'Connor concurring).

[8] Statement of Ronald A. Pearlman, made available at hearings on S.J. Res. 104 (retroactive taxation amendment) held before this subcommittee on August 4, 1994, at 2–3.

[9] *Id.* at 3.

[10] *Id.* at 7. See also the text at n. 11, *infra*.

take undue advantage of identified tax loopholes, thereby further increasing the deficit or requiring honest, taxpaying citizens to pay higher taxes in order to make up for advantages accruing to a few.[11]

Notice that in claiming that, on occasion, fairness may require "explicitly retroactive tax legislation"—which this amendment would preclude—Mr. Pearlman is claiming, by implication, that substantive unfairness should trump procedural unfairness—that we are permitted to engage in procedural unfairness in the name of correcting substantive unfairness. As a general principle, of course, that is a prescription for anarchy, and for the demise of the rule of law. But in the tax area, driven as it is by positive law, it is an invitation to congressional irresponsibility of the rankest kind.

Indeed, nowhere is that irresponsibility better presaged than in the very characterizations Mr. Pearlman invokes. He speaks, for example, of "abusive" tax shelters, tax shelters that by definition are legal—as is evidenced by the need for a change of law to "correct" them—but not quite what Congress had in mind when it drafted the law under which they arose. He then speaks of "perceived" abusers—as seen through the eyes of the American people—and of their taking "undue" advantage of "identified tax loopholes." We can never be sure, of course, just what advantage is "undue," especially since the law permits the advantage. We can be sure, however, about Mr. Pearlman's view of those who avail themselves of such advantages, for he contrasts them with "honest, taxpaying citizens," who must now pay higher taxes to make up for the shortfall caused by the "abusers."

Plainly, this substantive unfairness to other taxpayers is what exercises Mr. Pearlman, as well it should, particularly if one is concerned about threats to the income tax base, as he is. But in the end, his fire is misdirected, for it is not the "abusers" who wrote the law under which the alleged abuse takes place but the United States Congress. When Congress later tries, however, to correct substantive unfairness by being procedurally unfair to others—by changing the rules after the fact—not only does it compound the error but it does so deliberately. In the process, moreover, Congress often shifts responsibility from where it belongs—with itself—to where it does not belong—with others—ridiculing those individuals by holding them up to public obloquy as "abusers" of the system, even when their actions were, admittedly, legal. And it does so even in cases in which the individual, such as the executor in *Carlton*, was duty-bound to make the most he could of the estate he was charged with executing. For having complied with that duty, the executor in *Carlton* suffered a loss of $600,000 to the estate (not counting the tax itself plus interest), all due to a retroactive change in the law at the hands of Congress.

Thus, substantive unfairness, which is usually widely spread and small in any given case, is no justification for procedural unfairness, which is usually concentrated and large in individual cases. Nor will the effort to limit retroactivity to "closing loopholes" withstand scrutiny. Even those who generally oppose retroactivity are sometimes found trying to justify the practice in this limited way by distinguishing between "unfair" retroactive taxes—such as President Clinton's 1993 retroactive tax increase-and "fair" retroactive taxes—"technical corrections," often made a short time after the original "mistake" and often couched in the language of "closing loopholes."

The problems generally with retroactivity do not go away, of course, if its use is limited to this small area. What you have with this so-called fair retroactivity is really quite simple, in either of its forms. On one hand, Congress has made a mere technical mistake, which is not uncommon, but which individuals then rely upon as they order their affairs. In this case, we cannot ask individuals to try to ferret out Congress's "real" intent, which not even courts do well. Rather, we have to take the law as it is, and ask others to do the same. Indeed, in ordinary contract law we decide any ambiguity or drafting mistake against the drafting party on the grounds that it, not the other party, is responsible for the mistake and is in a better position to have avoided it. Those same grounds apply at least as strongly here.

On the other hand, the "mistake" Congress might make is one of carelessness in drafting such that shrewd individuals, accountants, and lawyers are able to "outsmart" the drafters, finding "loopholes" that hadn't occurred to Congress at the time of drafting. Here too, however, the issues remain the same. As Judge Learned Hand put it nearly 60 years ago, no one is obligated to arrange his affairs in a way that "will best pay the Treasury; there is not even a patriotic duty to increase one's taxes."[12]

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[11] *Id.* at 8.

[12] *Helvering* v. *Gregory*, 69 F. 2d 809. 810 (CA2 1934).

The deeper problem, of course, is Congress's use of the tax system for social planning. Just as the law of unintended consequences undermines direct attempts at social planning, so too it undermines indirect planning through the tax system. Man was born to be free. Try as governments might to plan a person's life through redistribution or regulation—or even through the tax code—he will find ways to regain control, to regain his freedom. That is a lesson that is being learned around the world, even if it is slow to come to the nation that should never have forgotten it.

Thus, I urge this subcommittee, Mr. Chairman, to erect an impenetrable barrier to retroactive taxation in all of its forms, which only a constitutional amendment will do. If the current draft of the new Russian Constitution can prohibit such taxation, as Article 57 of that draft does, we should be able to do no less.

Senator KYL. I am going to skip over Ms. Dixon now since Mr. Caplin is here. Mr. Caplin, we welcome you to the hearing as well. We have been going under a 7-minute rule which the Chair has not rigorously enforced, but I would make the point again that all written statements will be made a part of the record so you are free to summarize them if you would like to.

STATEMENT OF MORTIMER M. CAPLIN

Mr. CAPLIN. Thank you, Mr. Chairman. I first would like to apologize for my lateness here. I ran into an emergency that just held me up a few minutes.

Senator KYL. We appreciate your ability to be here.

Mr. CAPLIN. Thank you, Mr. Chairman. As you know, my name is Mortimer Caplin. I am with the Washington law firm of Caplin and Drysdale, and I had the privilege of serving as Commissioner of Internal Revenue during the 1961 to 1964 period under Presidents Kennedy and Johnson and I have been a tax practitioner for some 40 years.

I certainly sympathize with the vexation of constituents and Members of Congress over what they often perceive to be inappropriate retroactive legislation, but I don't think it wise to place a blanket constitutional prohibition, regardless of the circumstances, on Congress' ability to adopt retroactive legislation.

I would continue the existing flexibility in the normal legislative process so as to meet the needs and exigencies that may arise in our dynamic society, which include possible economic crises and threats to our national security, and also to preserve the integrity and administerability of the tax system.

The Supreme Court has allowed Congress the broadest of discretion in deciding when retroactivity is appropriate, and in exercising this discretion Congress, as well as the Treasury, have shown consistent sensitivity to the reasonable expectations of taxpayers and to fundamental concepts of fairness. Typically, they strive for legislation that is prospective. That is the norm in its most commonly understood sense; that is, applicable only to post-enactment transactions and events.

When a retroactive effective date is used, Congress has repeatedly followed the practice of, No. 1, alerting the public to its intention to adopt a particular provision of tax law and then tying retroactivity to that announced date. The date may take many forms—a Presidential budget message, a committee announcement, a press release, introduction of a specific bill, release of a committee report, or the date a bill is passed by both Houses.

On balance, Congress has demonstrated impressive self-restraint and concern for the man on the street's views. It has responded

regularly by providing grandfathering, exempting from adverse tax consequences transactions completed before the effective date, and even exempting non-completed transactions when a binding commitment is in place, and also by providing liberal, delayed, and phased-in effective dates, as well as other transition devices. The aim is to avoid hardship and claims of unfairness whenever practicable.

Now, Congress has been very generous in this regard. In fact, it is sometimes sharply criticized for excessive use of these transition rules. This is so when it is said to be done to buy votes for support of a particular piece of legislation. The targeted abuse here is the rifle-shot transition rule narrowly drawn to grant relief for a very specific taxpayer.

For the 1986 Tax Reform Act, a monumental piece of legislation, the Senate Finance Committee reported that it contained 650 rifle-shot transitional rules. According to the conservative estimate given by its then chairman, the cost was $10.6 billion in lost revenue, but it was nevertheless considered crucial to the passage of the Act and, in fact, other estimates run 2 or 3 times that size. Some wise commentator once said it is in the design of a transitional rule that the act of lobbying achieves its grandest moments, and we have certainly seen that.

I would like to say a few words about retroactivity. It is commonly regarded as applying new tax rules to already completed transactions, but economists and tax experts, including the Treasury, point out that all effective dates, including these nominally prospective dates, are indeed inherently retroactive.

Take legislation with a nominally prospective date, the effective date of the enactment, set at the beginning of the calendar year next following the date of enactment; let's say the following January 1, after some November legislation. Take, then, the owner of tax-free municipal bonds whose interest will become taxable prospectively only after the new effective date, or the owner of the home whose mortgage interest for the first time will be non-deductible prospectively after the new effective date, or the corporate executive whose long-accumulated deferred compensation will become payable or whose long-held appreciated asset is now planned for sale and who will be taxed prospectively after the new effective date of a rate increase. Realistically, it would have to be acknowledged that this nominally prospective effective date is in a very large sense retroactive in all these situations.

Despite this broad appraisal of retroactivity, tax laws must still strive to meet the American public's perception of fundamental fairness, honoring taxpayers' good-faith reliance on existing law and their abhorrence to changing the rules of the game midstream. These are important precepts. They are very important for the respect of our self-assessment system. I recognize that. Clearly, tax legislation, wherever possible, should have as a basic goal dates prospective in nature.

Having said this, however, and I close on this, I strongly urge that it would be unwise tax policy to simply tie the hands of Congress to flatly deny it the flexibility needed in a variety of circumstances to meet special fiscal demands of the Nation, and I can recall situations like that during the Vietnam War, or to counter

unanticipated abuses by taxpayers, and think of the horrible shelter period we had when billions and billions of dollars were lost, and to correct its own drafting errors or oversights.

In sum, Congress must have in hand all the necessary tools, including the option to use retroactive effective dates, not only to meet its own legislative responsibilities, but also to enable our administrators and courts to fulfill their assigned roles.

I have great faith in Congress. I think that most of the time they want to be fair and decent and they do make their legislation prospective in application. To the extent that congressional misuse of power or disregard of public expectation is perceived, fortunately in our democracy there is always the effective monitoring mechanism of the ballot box.

With that, I close and thank you.

Senator KYL. Thank you, Mr. Caplin.

[The prepared statement of Mr. Caplin follows:]

PREPARED STATEMENT OF MORTIMER M. CAPLIN

My name is Mortimer Caplin, a member of the Washington law firm of Caplin & Drysdale. I served as U.S. Commissioner of Internal Revenue from early 1961 to the Fall of 1964, during the Kennedy and Johnson years, and have specialized in tax law for over 40 years. It is a privilege to accept your invitation to testify at these hearings.

I sympathize with the vexation of constituents and members of Congress over what they often perceive to be inappropriate retroactive changes in the tax law. But I do not think it wise to place a blanket constitutional prohibition on Congress' ability to adopt tax legislation retroactive in some of its impact. I would continue the existing flexibility in the normal legislative process so as, first, to meet the needs and exigencies that may arise in our dynamic society—which include possible economic crises and threats to our national security—and, also, to preserve the integrity and administrability of our tax system.

For at least the past 50 years, Congress has made every effort to exercise its retroactivity power in a decent and reasonable manner; and, throughout, its actions have consistently been upheld by the Supreme Court. In fact, in no case in its history has the Supreme Court struck down an income tax provision on the grounds of retroactivity.

In decisions dating back to the 1920s, the court did deny retroactive application of an estate tax provision under the Revenue Act of 1918 and retroactive application of the first gift tax under the Revenue Act of 1924—although it is now almost universally agreed that the modern Supreme Court would not find unconstitutionality even in these cases. Indeed, in its most recent decisions, the court has given sweeping approval to retroactive amendments to three very different sections of the Internal Revenue Code—upholding the retroactive elimination of an estate tax deduction in *United States* v. *Carlton* (1994), the retroactive denial of a lifetime gift tax exemption in *United States* v. *Hemme* (1986), and the retroactive application of the amended minimum tax to a pre-enactment sale of real estate in *United States* v. *Darusmont* (1981).

Each of these decisions had its footing in the belief that Congress had acted reasonably and that the retroactivity was neither "harsh and oppressive" nor "arbitrary and irrational." Today, all the Court asks is that the retroactive application of the tax provision be "rationally related to a legitimate legislative purpose." And in the eyes of Justice O'Connor, at least, "it is sufficient for due process analysis if there exists some legitimate purpose underlying the retroactive provision". Raising revenue in an informed and balanced fashion certainly falls within this standard.*

In exercising this discretion, Congress as well as the Treasury have shown consistent sensitivity to the reasonable expectations of taxpayers and fundamental concepts of fairness. Typically, they strive for legislation that is prospective in its most

* In *Tate & Lyle. Inc.* v. *Comm'r*, 103 TC 656, 679 (1965), the plurality opinion found excessive ("violates the Due Process Clause") a 9-year retroactive reach of a legislative income tax regulation. Contrast this with the 14-month retroactivity period upheld in *U.S.* v. *Carlton*, 114 S. Ct. 2018 (1994).

commonly understood sense—that is, applicable only to post-enactment transactions and events.

RETROACTIVITY IN ACTION

On the eve of the adoption of the sweeping Tax Reform Act of 1986, House Ways and Means Chairman Dan Rostenkowski (D–IL) promised that the pending tax legislation would avoid "abrupt and arbitrary changes," observing that "no person should be penalized tomorrow for doing something that's perfectly permissible today." Shortly thereafter, he joined Senate Finance Committee Chairman Bob Packwood (R–OR) in stating, "we believe that the effective date of [the change] should not be inconsistent with the reasonable expectations [of taxpayers] based on law * * * in effect at the time the [asset] was purchased."

An interesting example of carefully balanced self-restraint is found in the 1950 revision of the formula for taxing life insurance companies which had paid little or no income taxes for 1947 through 1949. In 1949, a Joint Resolution was passed by both houses to impose taxes for all these years, but in the final 1950 Act the new rules were applied only to 1949 and 1950. As the Senate Finance Committee Report explained:

> Your committee does not believe it advisable to apply the formula retroactively to the years 1947 and 1948. The returns for those years were filed some time ago; the books of the companies have been closed; and in some cases no reserves were established to cover the Federal tax liability * * * [S]ome companies had made commitments in those years relying on the fact that no Federal income tax was payable under existing law. Hence, the payment of the tax now could impose a hardship upon the policyholders.

This is consistent with a common congressional practice of alerting the public to its intention to adopt a particular provision of tax law, and then tying any retroactivity to the date of the announcement. The date may take many forms—a presidential budget message, a committee announcement or press release, the introduction of a specific bill, the release of a committee report, or the date a bill is passed by both houses.

Patterns of retroactivity employed by Congress have previously been analyzed in great detail:**

1. Legislation is commonly made retroactive to the beginning of the year of enactment. At times, too, there are provisions enacted shortly after the end of the first year to which they are retroactively made applicable.

2. Provisions which are nominally prospective only will frequently have future application to transactions irrevocably entered into years previously. In contrast, Congress will at times exempt situations entirely when before the date of enactment, transactions had been completely culminated or even where only binding contracts or other commitments had been made.

3. Retroactivity may be employed to eliminate a "loophole" or "unintended benefit," although even here—depending upon the egregiousness or the revenue loss at stake—Congress leans towards post-enactment application.

4. Retroactivity is at times adopted to correct technical errors in prior legislation—"technical," "clerical," "typographical," or "grammatical" errors. Related to this is the so-called "clarifying" amendment, made to "reflect" a supposed "Congressional intent," which is usually made retroactive but may be made prospective when doubt exists about the meaning of the prior law.

5. Mention should also be made of legislation which confers a benefit on taxpayers or corrects hardships inadvertently created in previously enacted legislation. Here retroactivity is generally considered unobjectionable, although recognition must be given to the cost-shifting effect of the overall burden on other taxpayers.

On balance, Congress has demonstrated impressive self-restraint and concern for the man-in-the-street's views on what is regarded as retroactivity, and what is fair and reasonable under existing circumstances. It has responded regularly (1) by providing for "grandfathering"—exempting from adverse tax consequences transactions completed before the effective date and even exempting non-completed transactions when binding commitments are in place, and also (2) by providing liberal delayed and phased-in effective dates, as well as other transition devices. The aim is to avoid hardship and claims of unfairness whenever practicable. Not that it has always been successful in the eyes of the public. Under the 1986 Tax Reform Act, for example, broadscale criticism was made of its failure to grandfather or provide

** Laurens Williams, *Retroactivity in the Federal Tax Field*, 12 U.S.C. Law School Tax Inst. 79 (1960) (former Assistant Secretary of the Treasury and Head of Legal Advisory Staff).

stronger transition relief for numerous locked-in positions taken under preexisting law.

Congress has generally been very generous. In fact, it sometimes finds itself sharply criticized for making excessive use of these transition rules. This is so when it is said to be done to buy votes for support of a particular piece of legislation. The targeted abuse here is the "rifle-shot" transition rule, narrowly drawn to grant relief for a very specific taxpayer. For the 1986 Tax Reform Act, the Senate Finance Committee reported that it contained 650 rifle-shot transitional rules. According to the conservative estimate of its then chairman, the cost was $10.6 billion in lost revenue, but it was nevertheless considered critical to the passage of the Act. Other estimates run two and three times higher.

Senator Carl Levin (D–MI.) referred to them as "nothing less than a tax break for a special company". Playing on this theme, the then Assistant Treasury Secretary for Tax Policy ruefully observed, "This is something less than the finest demonstration of democracy in action, but I regard it as the price of reform." And in mock admiration, still another has said that it is "in the design of transitional rules that the act of lobbying achieves its grandest moments."

RETROACTIVITY DEFINED

I would like to say a few words about what we mean by "retroactivity."

Retroactivity is commonly regarded as applying new tax rules to already completed transactions. But economists and tax experts, including the Treasury Department, point out that all effective dates—including those nominally prospective—are indeed inherently retroactive.

Take tax legislation with a nominally prospective effective date set at the beginning of the calendar year next following the date of enactment. Take then the owner of tax free municipal bonds whose interest will become taxable prospectively only after the new effective date; or the owner of a home whose mortgage interest for the first time will become non-deductible prospectively after the new effective date; or the corporate executive whose long accumulated deferred compensation will become payable, or whose long-held appreciated asset is now planned for sale, and who will be taxed prospectively after the new effective date of a rate increase. Realistically, it would have to be acknowledged that this nominally prospective effective date is in a very large sense retroactive in all these situations.

Professor Michael Graetz has ably shown why, practically speaking, all effective dates have a retroactive impact:***

> Because all changes in law, whether nominally retroactive or nominally prospective, will have an economic impact on the value of existing assets or on existing expectations, the distinctions commonly drawn between retroactive and prospective effective dates are illusory. * * * Therefore, purportedly prospective changes in the law that alter people's expectations about their earning prospects or their potential savings or consumption, or, as is very often the case, alter the value of an asset * * * have retroactive effects. Understood this way, all changes in law—indeed, I think, all changes in economic laws—are inherently retroactive.

Supreme Court Justice Harry Blackmun, in his recent majority opinion in the *Carlton* case, subscribed to this view in noting, "An entirely prospective change in the law may disturb the relied-upon expectation of individuals, but such a change would not be deemed therefore to be violative of due process."

Despite this broad appraisal of retroactivity, tax laws must strive to meet the American public's perception of fundamental fairness—honoring taxpayers' good faith reliance on existing law and their abhorrence to changing the rules-of-the-game midstream. "Bait-and-switch" taxation has already been roundly criticized, and it might not be a bad idea to pin large posters on the walls exclaiming: "Do not take taxpayers by surprise." "Respect taxpayers' prior reliance and irrevocable changes of position." "Give taxpayers advance notice of congressional plans and projected dates for tax law changes." These are all important precepts in building respect and confidence in our voluntary self-assessment system. And, clearly, tax legislation whenever possible should have as a basic goal effective dates prospective in nature, not retroactive in the sense generally understood.

Having said this, however, I strongly urge that it would be unwise tax policy to simply tie the hands of Congress—to flatly deny it the flexibility needed in a variety of circumstances, (1) to meet special fiscal demands of the nation, (2) to counter unanticipated abuses by taxpayers, and (3) to correct its own drafting errors and over-

*** Michael J. Graetz, Retroactivity Revisited, 98 HARV. L. REV. 1820, 1822 (1985).

sights. In sum, Congress must have in hand all the necessary tools—including the option to use retroactive effective dates—not only to meet its own legislative responsibilities, but also to enable our tax administrators and our courts to fulfill their assigned roles in an efficient and reasonable fashion.

I have faith and confidence in the good judgment and essential fairness of Congress. But to the extent congressional misuse of power or disregard of public expectations is perceived, fortunately in our democracy there is always the monitoring mechanism of the ballot box.

MORTIMER CAPLIN,
Washington, DC.

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Senator KYL. Our last witness—I could say we are saving the best for last—is Ms. Joanne Dixon. The floor is yours.

STATEMENT OF JOANNE DIXON

Ms. DIXON. Thank you. Mr. Chairman, Members of the subcommittee, and especially my Senator Coverdell, thank you for inviting me to testify today about S.J. Resolution 8, the proposed constitutional amendment to ban retroactive taxes.

My name is Joanne Dixon, and I have been overwhelmed by all of this knowledge and power in the room. I have been sitting here trying to figure who I am, what I am doing here, and what is this all about.

Senator KYL. Ms. Dixon, the two of us work for you.

Senator COVERDELL. That is right.

Ms. DIXON. I understand that. Yes, I know that, but being introduced as Joanne Dixon, Jirard, GA—no one knows where Jirard is, so I just decided I am also a mother and I am also an ex-farm wife, and both of those play a tremendous part of this hearing today, for without a mother none of us would be here, and farmers grow the food that fuels the world. So now you know how important I am, right? These guys just know it all, but I had a great portion to do with our presence here today. So now I will move on. Thank you.

My husband, Jimmy, and I were farmers for 38 years in rural Georgia and we were harmed by the retroactive tax increase contained in the 1993 Omnibus Budget Reconciliation Act. I appreciate the opportunity to share my story with you and to put a face to the many people I believe who exist who were also hurt by retroactive taxes.

My husband, Jimmy, and I were married in August 1955. We farmed together since then until 1993 and it was the only life that we had ever known. I believe that we were responsible citizens and, like our neighbors, we farmed our land, went to church, contributed to our community and paid our taxes. We were proud to be farmers and we believed it to be a very good life.

In February 1993, my husband suffered a second heart attack. He survived, thank God, but we knew that our life farming the land together was over after 38 years. The physical demands and the stress with running a farm were just too much for Jimmy. There was no time to consider another alternative method or way or life. His life literally was at risk and we could not continue. It was a gut-wrenching decision. That was February, the time of the year when the wheat already was planted and plans were underway to farm 2,000 acres for another year.

Jimmy had to have angioplasty after the second heart attack, and there we were having to face the most traumatic experience ever. We had to auction off everything we had worked for our entire lives. I could never put our feelings into words to adequately express what we went through. I will never forget the day of the auction itself. Looking back, I really don't know how we stood it, but we did manage. Soon after, we had to sell the livestock on the farm because the cattle were calving at the time and Jimmy and I just could not handle this alone.

We had a wheat crop, 2,000 acres ready to farm and a large portion of our equipment was set up on a lease/purchase arrangement, and we also had a leased irrigation system. While we used the proceeds of the auction to pay these leases off and to pay the auctioneer his percentage, this counted as income. In addition, we sold crops in January that were harvested in 1992. The funds from selling these we call carryover crops were intended to provide the cash-flow necessary to prepare for spring planting, but they still counted as a part of our income.

On this income, we dutifully paid income tax and capital gains tax. Then we were forced to relive this painful period of our lives because we had to pay still more in retroactive taxes based on the income from liquidating the only life that we ever knew. The amount of money itself was not a large amount, but we still had to pay the retroactive tax out of funds we had planned then for retirement. However, for me, that is not the issue.

After what we had been through and what we had already paid, about equal to what we had worked for our entire lives, to know that the Federal Government can tax you simply because it chooses was a real shock. I truly believe that if our tax bill had been more, it could have brought on another heart attack for Jimmy. It could have cost his life.

Furthermore, our situation also left us with no way to recover this money we had to pay in this additional tax. We were out of business. The retroactive tax was a shameful tax. The only protection I believe people like me would have is to amend the Constitution to ensure it never happens again. I wholeheartedly support Senator Coverdell's proposed amendment.

Thank you very much.

Senator KYL. Thank you very much, Ms. Dixon. It is interesting that Ms. Dixon kept to the time limits, while none of the rest of us have.

Ms. DIXON. I really wanted to say if I had gone first, I would yield my time.

Senator KYL. Thank you all for your testimony.

Senator Coverdell, would you like to begin the questioning?

Senator COVERDELL. I want to thank all the panelists for taking their time to be here and sharing their thoughts with us.

To Mr. SCHMITZ AND DR. Pilon, I would just add you have eloquently covered *ex post facto* and due process, but I would say there is a third provision and I would welcome you to review it, and it is bills of attainder. If you go back and you visit the debate over the retroactive taxation—and I would suggest this probably happens in others, as well, of retroactive taxation—it is clear time and time again that certain classes of citizens will theoretically be subjects of the retroactive tax attempt. I think the Constitution addresses that under "no bill of attainder."

So I think there are three provisions of the Constitution—*ex post facto*, due process, and bills of attainder—that deal with this subject matter. As I said in my opening statement, I think the Constitution pointed in every way it knew to suggest that this was not an acceptable concept.

To Mr. Caplin, a question, and hopefully in this exchange we point to the problem here. What would have been the notice in this particular case of retroactive taxation? Was it the President's campaign where he said taxes would be lowered? Was it his State of the Union where he said the middle class will be asked to make a contribution? Was it the nature of the debate, for which no one could determine from day to day which piece would or would not be a part of the law?

I can't for the life of me think of any way for which you could conclude that President Bush should have been—or something he said, the appropriate notice, where not only did the Congress, working off the various notices that were coming from the new chief executive—it is beyond me how you could ever reach back into a prior administration.

Mr. CAPLIN. You say a prior administration?

Senator COVERDELL. Right.

Mr. CAPLIN. I have never heard of a situation like that, really. You know, I can't think of a case like that, but I think in a given

period of time, let's say, whether the Democrats were in control or the Republicans, there have been instances when specific legislation has been proposed during the tax shelter era when the tax court was just clogged up with tens of thousands of cases, 50,000, 60,000 cases clogged up there, and corrective legislation was proposed as part of a large bill, but it held over and they announced an effective date. They announced the effective date in the committee, not a Presidential message. Then the legislation was finally passed a year or so later, but they did block the shelters during that period of time.

Now, if that hadn't happened, the committee reports normally give you a blueprint of exactly what you should do. I mean, if you want to really specialize in tax avoidance, read the committee blueprint, the joint committee staff analyses where they tell you exactly what the problem is. Then if the legislation is passed a year later, I mean you have lost billions of dollars. I mean, this is the last chance to get on board and people flock to that.

So I mean it is rare for a Presidential message. I don't know if this is exact, but there was a tax message given. I know President Kennedy gave a tax message. Now, I don't recall whether he announced any effective date in that, but that would have been the type of instance, something very specific.

Senator COVERDELL. I would just argue in this most recent case it is particularly egregious because not only can you not fix a date, but the messages are absolutely incongruous that were being sent to the American people. I would also say that the dilemma that Ms. Dixon and her husband found themselves in—now, you are a tax attorney and have deep understanding. You are a Washington resident with past Government service, but I would simply argue that the vast majority of Americans are in the situation of the Dixons and I think it is an undue burden to think that they—the law firms understand, but the vast majority of our people can't even begin to work off the suggestion that there is an announcement in the Finance Committee or in the Tax Committee.

I think, also—and this is a point on which we disagree—that you are making an argument I have heard—I have only been here 36 months, but I hear it often. It is the same argument for not having a balanced budget amendment to the Constitution; that is that the Congress ought to have the flexibility and it can make the prudent decisions. But I think the American people are at a point where they want more protection and have become increasingly, and I think understandably disillusioned with that flexibility, which has, I think, been ably described by Ms. Dixon.

I know in some conversations there was another individual who would come under bill of attainder because of his success, but somebody you knew about that had to pay a huge sum of——

Ms. DIXON. One hundred and eighty thousand dollars.

Senator COVERDELL. One hundred and eighty thousand dollars of retroactive taxes?

Ms. DIXON. Of retroactive taxes.

Senator COVERDELL. I would say that would affect anybody.

Ms. DIXON. Well, it affected everyone because he owned fast food restaurants, so middle America paid for that when they bought hamburgers or whatever. He could make his up.

Senator COVERDELL. But somebody paid for it.

If you don't mind, Mr. Chairman, her husband to whom she has been referring is here, Commissioner Jimmy Dixon, and we are glad you have survived these incidents so well. I think we ought to at least acknowledge him.

Senator KYL. I was going to say it is good to see you here in view of the health difficulty that you had, and I am sure that it was adding insult to injury when you had this obligation to the Federal Government after these health difficulties.

Dr. Pilon seemed to want to make one other comment in response.

Mr. PILON. Yes. In listening to Mr. Caplin responding to Senator Coverdell's question, I was struck by the picture of Mr. and Mrs. Dixon poring over committee blueprints, as he put them, and wondered when they would have time to plant the crops as they were poring through these oftentimes voluminous records to keep up with the latest in tax law. This is the kind of inside-the-Beltway picture that we are invited to believe substitutes as notice in these matters and I think you have put your finger exactly on the point, Senator Coverdell.

The average American just is not sitting around following the latest missives from Congress to rearrange his affairs so that he can thereby avoid taxes. The world doesn't work that way, and you know it, of course. I think that the arguments that purport to tell us that it does just simply miss the real life. Mr. and Mrs. Dixon have to live their lives, get on with their lives, and they have to arrange their affairs with respect to broad notice, and I think you hit it exactly right.

Were we to take the Mr. Clinton of the campaign, the Mr. Clinton of the inaugural address, the Mr. Clinton later on down the road, which statements of those—often contradictory statements—are we to repair to by way of gaining notice of what is going on?

Senator KYL. Even in situations where—I will give you an opportunity to respond in just a minute on my time. How is that?

Mr. CAPLIN. Thank you.

Senator KYL. The capital gains tax reduction that was supposed to take place—constituents asked me what the effective date was. Senator Coverdell will recall one of the effective dates was going to be January 1, 1995. Another effective date was going to be January 1, 1996. Another effective date was going to be the date of enactment, and there were two or three other potential effective dates. Every time I would go home, constituents would say, well, what is going to be the effective date of this? Nobody could say, and in the end it didn't even pass.

Mr. Caplin, the one thing I would like to say about your testimony is that I think that much of your discussion about transition rules designed to protect people would not be proscribed by this amendment because it is not the imposition of a tax, but rather relieving someone of a tax burden, at least for a while. The wording of the amendment provides, "No Federal tax shall be imposed for the period before the date of enactment of a tax."

So, clearly, where you need to allow for a transition to a new kind of tax code, we are going to be providing people an opportunity to make changes before the new tax is actually applied. But

I don't think the intent here is to preclude us from being able to help people with these transition rules, but rather to make it more difficult for us to go back in time at a point in time when they were not able to change their behavior.

You see, the retroactive tax on the Dixons here they could never have done anything about. There was never a notice given to them in time for them to do something about it. The tax was actually made retroactive to a point earlier than the time the Congress even began the debate on the proposal, technically even before the administration took office. So there was no way for anybody to change their behavior even with a notice later on. I think that is the primary thing we are trying to deal with here.

Mr. CAPLIN. I am very sympathetic to Ms. Dixon. I think almost anybody would have to be. I am not particularly familiar with the exact transaction she is talking about as to what was retroactive as of what date.

When I am talking about the Chairman of the House Ways and Means Committee announcing that capital gains shall be lessened as of January 1, 1995, I would regard that as a rather specific commitment, and it isn't just in the Beltway. Typically, newspapers around the country pick this thing up pretty broadly.

Senator KYL. But it didn't happen.

Mr. CAPLIN. That is right.

Senator KYL. Therefore, somebody going ahead and selling an asset based on that certainly——

Mr. CAPLIN. Yes. I would have been very cautious about that under the circumstances. That is right, that is right. It is a very difficult situation. There are hardships. I mean, even today the last piece of a transition rule was taken care of. Personal interest was made non-deductible and over a 3-year period they allowed for some transition device. You wouldn't have to pay the full tax in 1 year. Congress, in its wisdom, used a 3-year period.

I abhor retroactivity. I gave you examples of really true retroactivity that wouldn't be covered by your bill, as I understand it. I mean, the fact that I had deferred compensation for my entire life as a lawyer to be paid to me after my retirement next year and you make an effective date today—I am now going to have higher rates that next day. I mean, what about protecting me? I mean, I have a lifetime tied up in my pension plan.

I just feel that I would come and try to convince you somehow that you have to give me some relief and leave it to your good judgment and wisdom. The question of what would compel the majority of Congress to make a bill retroactive—there has to be some strong needs.

Senator KYL. Yes; the need for revenue. I am not sure that is strong enough.

If I could, because the time is short here, I think one can argue making—well, making perfection an enemy of the good is another way to say it. There will always be effects on people as a result of what we do, but there is a difference in magnitude, it seems to me, between the error that we propound when we announce an effective date some time into the future as opposed to going back in time when people don't have any opportunity to do anything to alleviate that particular burden. We are addressing the latter, not

the former. We can't solve everything or we would—as Dr. Pilon said, the argument, in a sense, proves too much. We would be precluded from acting at all.

I also want to say to Joe Schmitz that this is not the only subject upon which I am familiar with his writings. He has written extensively on a variety of constitutional issues, including a recent piece on the tenth amendment, and I think his statement about the history of this issue will be particularly informative to the record because it is apparent that the Supreme Court is not going to change the law any time soon.

I was going to ask you what it would take, but I gather it is not in the cards. I think we can just summarize it that way. Therefore, this very extensive and interesting historical perspective which you have provided will enable us, the Congress, to make the change that it appears to me the Court simply doesn't have the stomach for.

I am interested at this point, as I am sure Senator Coverdell is, in getting any other judgments as to precisely how we can best do this, assuming that we want to do it, to deal with the problems and issues that have been raised. But I think the historical record that Joe Schmitz writes about and that Dr. Pilon has testified about makes it crystal clear that it was the original intent of the Framers. So if the Court isn't going to do it, we have got to do it and the question is how best to do it. Rather than raising all kinds of burdens about why it is hard, I think we ought to be focusing on how we can make it happen.

Now, given the fact that we have about another 7 minutes here, if Senator Coverdell would like to engage in another round of questioning or make any comments or if any of the other witnesses would like to add something, I would afford you that opportunity.

Senator COVERDELL. I will defer to the witnesses and the Chairman, other than to say that I think the national security issue could be rather comfortably dealt with. Perhaps that is a reason to override, but that would not be inordinately difficult in our language to deal with in terms of if there were a hostile conflict that called on the Congress. Some of the retroactive taxation has actually been directed at resolution of those kinds of matters.

The one with which we are mostly currently dealing is egregiously absent any national security and really only relates to national spending priorities. But if we could all come together, taking your admonishment, and work toward perfection of it, I think we can produce something that eliminates all but the intellectualizing in terms of what ultimate flexibility might enable us to do, which I reject, but I will stop with that, Mr. Chairman.

Senator KYL. Well, may I just ask one final question, then, of any of you? I guess I will address it to you, Mr. Caplin, but I would like to get Joe Schmitz' reaction to this, too.

Am I correct that transition rules designed to allow people not to be taxed for a period of time until they can get their affairs in order to comply with a new provision in the code—that that would not be proscribed by this particular provision? Am I correct in that?

Mr. SCHMITZ. I would say definitely that would not be covered by the prohibition. I mean, there is a fundamental difference between taking property away from a citizen and allowing the citizen to

keep his own property. You know, we talk about tax breaks and, you know, we have to ultimately face the fact that taxation is taking money from individuals or companies. It is a fundamental power that a sovereign has.

You know, when we go back to Blackstone, if I could just refer back to the 18th century again, Blackstone defined four essential elements of any civil law, and I will just read it. This is right out of what the constitutional Framers cited in the debate over the *Ex Post Facto* Clause and due process provisions. Blackstone says that a civil law is, "a rule of civil conduct prescribed by the supreme power of a State."

Now, we have two problems we have to deal with today. One is sort of the elementary, fundamental problem about prescription. I mean, it is just so fundamental of any rule. You have got to write the laws and you have got to write them in advance of when they apply. I mean, the idea of a retroactive tax is just so abhorrent, as I said, and I can't imagine our Founding Fathers even listening to this debate without being completely disgusted that we are even sitting here having to debate this.

The other problem actually comes right out of Blackstone's definition, too, that these rules have to be prescribed by the supreme power of a State. Essentially, our retroactivity laws now are prescribed by the Supreme Court, which is not supposed to have any legislative power at all. In this regard, I would like to compliment Senator Kyl for cosponsoring a current proposal that would essentially try to wrest some of this power back to the legislative body.

There was a bill, if you don't mind, Senator Kyl, introduced on March 20, last month, called the Tenth Amendment Enforcement Act of 1996, which provides a very simple rule of construction for the courts. It says, "Any ambiguity in this Act or in any other law of the United States shall be construed in favor of preserving the authority of the States and the people." That is exactly what the Court doesn't do now, especially in the tax area.

Correct me if I am wrong, Mr. Caplin. Any ambiguity in the tax law, by Court edict, gets construed against the individual.

Mr. CAPLIN. That is not quite accurate, really.

Senator KYL. What is the general rule?

Mr. CAPLIN. Well, I think you will find the Supreme Court and lower courts will interpret them the other way. Frequently, it is the level of advocacy that has been involved.

Senator KYL. There are some general rules of interpretation, though, are there not?

Mr. CAPLIN. I really don't think so.

Senator KYL. Well, we don't need to debate that here.

Mr. CAPLIN. Right, right.

Senator KYL. I had promised that we would be done by 2:30. Dr. Pilon has a last comment. If I could ask you and then we will adjourn.

Mr. PILON. I would just say in response to Mr. Caplin the history of the courts' interpretation is not the kind of thing that would encourage the taxpayer. The point that you raised, though, Senator Kyl, about transition rules and periods and a period of time for people to get their economic affairs in order under new conditions

that may be emerging and to go without being taxed during that period is, I think, a very important issue.

It came up a little over a year-and-a-half ago when we held hearings on Senator Coverdell's bill in August 1994. It came up in the form of testimony that was put forward by Mr. Ronald Pearlman during that time, and the fear seems to be on the part of opponents of this amendment that it would result in some loss of revenue flow to the Government, which some people think is a bad thing.

There, it seems to me that the Government has to simply bite the bullet and say, yes, we are going to have to suffer some revenue loss as a result of mistakes that we may have made or changes that we want to make in the name of fairness; that is to say, as long as you think of the taxing situation as a zero-sum game where someone else's relief for a brief period of time means that someone else is going to have to pay more, then you will never get out of this conundrum.

You have got to stop thinking of it as a zero-sum game and start thinking of it as a game in which we are going to start rolling back taxes, returning power and the ability to keep their own money to the American citizen. Once you do that, then the so-called transition problem becomes far, far less. I think that the distinction that you made earlier on is absolutely to be focused upon; namely, changing the rules in the middle of the game versus changing the rules retrospectively. It is bad enough that you are going to have to change the rules in the middle of the game.

We have gotten ourselves into this gargantuan taxation situation, as Senator Coverdell mentioned in his testimony, and now we have the problem of getting ourselves out of it. It is a little bit like the Soviet Union and Russia today getting itself out of the massive socialism and all the problems that attend that it got itself into. People are going to be hurt in the process of getting out of this problem.

The idea is, though, that if you do it with a distinction between changing the rules in the middle of the game versus changing the rules retrospectively, that is extremely important to preserve that distinction and under no condition should you tax retrospectively even if you have to incur some burdens or impose some burdens upon people as a result of changing the rules in the middle of the game, which is what you are going to have to do under any circumstances.

Senator KYL. Mr. Caplin has one very short remark, please, and then Senator Coverdell.

Mr. CAPLIN. I want to say this here that I am strongly opposed to retroactive legislation and I would do everything I could to avoid it, but I was really making the argument for flexibility to take care of the emergency, the threat to our national security, any other crisis that might arise.

If you want to have the perfect world in terms of having pure prospective legislation, you have to think seriously of something that is more than the typical retroactive legislation. The man who has invested his fortune in real estate on the supposition that there are going to be certain deductions that he will be able to take year after year and he cannot change it without maybe bankrupting himself, selling that property at a bad price because the value of

the property probably will go down if the deductions aren't there—just like your own home; if you don't get the deduction for taxes that you pay in connection with your house, the value of that house is going to go down. So I think if you are going to think of this entire problem, you have to think of the locked-in position already.

Senator KYL. It sounds like a good argument for the flat tax.

Senator COVERDELL. Well, I would only argue that this would correct a portion of the egregious nature of changes of the rules in midstream and that we ought not to take other unsolved problems which ought to be aired here and let that be the argument for not making the fundamental change.

I am sitting here as I have heard this and I am thinking of the vast court of public opinion of the American people. If you put the question to them, now, let's see, should we amend the Constitution so that there shall be no retroactive taxation or should we protect the Congress from the foible of making a mistake and not being able to go back and correct it and modify it, you would want to get out of the way of the answer, it would be so forceful.

I thought your analogy of the schoolyard was very appropriate. I can remember those schoolyards and I can remember—I know you have all heard this—you are changing the rules; that is not what the rule was. It is fundamental. This is a fundamental transgression of American fundamental concept of fairness wherever the flag flies. I close on that.

Senator KYL. Thank you. That is a great statement to close on. Again, we thank all of the members of the panel for being here. I would like to notify everyone that the record of this subcommittee hearing will be kept open for 2 days for the submission of any statements on this amendment.

The hearing is now closed.

[Whereupon, at 2:34 p.m., the subcommittee was adjourned.]

APPENDIX

PROPOSED LEGISLATION II

104TH CONGRESS
1ST SESSION

S. J. RES. 8

Proposing an amendment to the Constitution of the United States to prohibit retroactive increases in taxes.

IN THE SENATE OF THE UNITED STATES

JANUARY 4, 1995

Mr. COVERDELL (for himself, Mrs. HUTCHISON, Mr. SMITH, Mr. LOTT, Mr. HELMS, Mr. KEMPTHORNE, Mr. CRAIG, Mr. SHELBY, Mr. MCCAIN, Mr. WARNER, and Mr. ROTH) introduced the following joint resolution; which was read twice and referred to the Committee on the Judiciary

JOINT RESOLUTION

Proposing an amendment to the Constitution of the United States to prohibit retroactive increases in taxes.

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled (two-thirds of each House concurring therein), That the following article is proposed as an amendment to the Constitution of the United States, which shall be valid to all intents and purposes as part of the Constitution when ratified by the legislatures of three-fourths of the several States within seven years from the date of its submission by the Congress:

"ARTICLE —

"SECTION 1. No Federal tax shall be imposed for the period before the date of enactment of the tax.

"SECTION 2. This article shall take effect the date of its ratification.".

II

104TH CONGRESS
2D SESSION

S. J. RES. 49

Proposing an amendment to the Constitution of the United States to require two-thirds majorities for bills increasing taxes.

IN THE SENATE OF THE UNITED STATES

FEBRUARY 27 (legislative day, FEBRUARY 23), 1996

Mr. KYL (for himself, Mr. COVERDELL, Mr. CRAIG, Mr. FAIRCLOTH, Mr. GRAMS, Mr. INHOFE, Mr. KEMPTHORNE, Mr. LOTT, Mr. MCCAIN, Mr. PRESSLER, Mr. SANTORUM, Mr. SHELBY, Mr. SMITH, Mr. THOMAS, and Mr. THOMPSON) introduced the following joint resolution; which was read twice and referred to the Committee on the Judiciary

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JOINT RESOLUTION

Proposing an amendment to the Constitution of the United States to require two-thirds majorities for bills increasing taxes.

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States within seven years after the date of its submission by the Congress:

"ARTICLE —

"SECTION 1. Any bill to levy a new tax or increase the rate or base of any tax may pass only by a two-thirds majority of the whole number of each House of Congress.

"SECTION 2. The Congress may waive section 1 when a declaration of war is in effect. The Congress may also waive section 1 when the United States is engaged in military conflict which causes an imminent and serious threat to national security and is so declared by a joint resolution, adopted by a majority of the whole number of each House, which becomes law. Any provision of law which would, standing alone, be subject to section 1 but for this section and which becomes law pursuant to such a waiver shall be effective for not longer than 2 years.

"SECTION 3. All votes taken by the House of Representatives or the Senate under this article shall be determined by yeas and nays and the names of persons voting for and against shall be entered on the Journal of each House respectively.".

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